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8599  
No. 12338

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United States  
Court of Appeals  
For the Ninth Circuit.

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NORTHWESTERN MUTUAL FIRE ASSOCIA-  
TION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

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Transcript of Record

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Upon Petition to Review a Decision of the Tax Court  
of the United States

FILED

NOV 25 1949

PAUL P. O'BRIEN, CLERK





No. 12338

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United States  
Court of Appeals  
For the Ninth Circuit.

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## APPEARANCES

For Petitioner:

JO D. COOK, ESQ.,  
1401 Joseph Vance Building,  
Seattle, Washington.

For Respondent:

WILFORD H. PAYNE, ESQ.



Docket No. 16147

NORTHWESTERN MUTUAL FIRE ASSOCI-  
ATION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

## DOCKET ENTRIES

1947

- Oct. 14—Petition received and filed. Taxpayer notified. Fee paid.
- Oct. 14—Request for Circuit hearing in Seattle, Washington filed by taxpayer. 11/13/47 granted.
- Oct. 16—Copy of petition served on General Counsel.
- Nov. 20—Answer filed by General Counsel.
- Nov. 20—Request for hearing in Seattle, Washington filed by General Counsel.
- Dec. 3—Copy of answer and request served on taxpayer—Seattle, Washington.
- Dec. 11—Entry of appearance of Jo D. Cook as counsel filed.

1948

- Mar. 23—Hearing set May 17, 1948, at Seattle, Washington.
- May 17—Hearing had before Judge Black on merits. Stipulation of facts filed at hearing. Briefs due 7/5/48—replies 7/25/48.

1948

- July 6—Brief filed by taxpayer.
- July 6—Motion for extension to July 22, 1948, to file brief filed by General Counsel. 7/7/48 granted.
- July 23—Transcript of hearing of 5/17/48 filed.
- July 27—Motion for leave to file the attached brief, brief lodged, filed by General Counsel. 7/27/48 granted and served 7/28/48.
- July 28—Petitioner's brief served on General Counsel.
- Aug. 16—Motion for extension to August 31, 1948, to file reply brief filed by taxpayer. 8/17/48 granted.
- Aug. 26—Motion for leave to file reply brief, reply brief lodged, filed by General Counsel. 8/30/48 granted.
- Aug. 30—Reply brief filed by taxpayer—copy served.

1949

- Mar. 30—Opinion rendered, Black J. Decision will be entered for the respondent. 3/30/49 copy served.
- Mar. 30—Decision entered, Black J. Div. 15.
- June 24—Petition for review by U. S. Court of Appeals, Ninth Circuit, with assignments of error filed by taxpayer.
- June 24—Proof of service filed.
- Aug. 3—Agreed motion to enlarge time to Sept. 2, 1949, to prepare and transmit record filed.
- Aug. 3—Order enlarging time to Sept. 22, 1949, to prepare and transmit record entered.

1949

Aug. 4—Stipulation that the record on appeal include all of the pleadings, stipulations and documents of record in the above Court (The Tax Court of the United States) filed.

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The Tax Court of the United States

Docket No. 16147

NORTHWESTERN MUTUAL FIRE ASSOCI-  
ATION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiencies set forth by the Commissioner of Internal Revenue in his notice of deficiency IT:90D:FCH dated July 18, 1947, and petitions for a redetermination of petitioner's claims for refunds, and as a basis of his proceeding alleges as follows:

1. That petitioner is a mutual fire insurance corporation organized and operating under the laws of the State of Washington, and is duly authorized and engaged in the business of writing insurance against the perils of fire and allied lines in all states of the United States and all of the mainland Provinces

of Canada, with its principal office at 217 Pine Street, Seattle, Washington; that the returns for the periods here involved were filed with the Collector for the District of Washington, at Tacoma, Washington.

2. That the notice of deficiency with statement attached, (a copy of which is attached and marked Exhibit A) was mailed to the petitioner on July 18, 1947.

3. That the taxes in controversy are income taxes for the calendar years 1942 and 1943 and the amounts in dispute are as follows:

a. For the year 1942 the Commissioner asserts a deficiency of \$5,089.03; whereas for said year petitioner claims a refund of \$10,183.13;

b. For the year 1943 the Commissioner asserts a deficiency of \$5,347.81; whereas for said year petitioner claims a refund of \$10,854.73.

4. That the determination of taxes set forth in the said notice of deficiency is based upon the following error:

The refusal of the respondent to allow credit under Section 131 of the Internal Revenue Code for taxes paid by the petitioner to the Dominion of Canada in lieu of income taxes.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

a. That petitioner made a timely filing of 1942



and 1943 income tax returns on Form 1120 M; that said returns were made on the accrual basis, and that in said returns foreign tax credits were claimed as follows:

(1) For the year 1942 a foreign tax credit of \$5,076.60 was claimed;

(2) For the year 1943 a foreign tax credit of \$5,339.84 was claimed.

b. That upon audit of the petitioner's tax returns for 1942 and 1943 the petitioner's tax, without deduction for foreign tax credit, was established at:

(1) \$67,163.21 for the year 1942;

(2) \$70,450.68 for the year 1943.

c. That petitioner filed timely claims for refunds of 1942 and 1943 income taxes paid; that petitioner's claims for refunds in 1942 and 1943 were made because petitioner did not claim credit on petitioner's original returns for the full amount of Canadian taxes paid by petitioner during said periods because petitioner made an error in the calculation of the limitations on the foreign tax credit; that petitioner's claims for refunds were as follows:

(1) For the year 1942 petitioner claimed an additional foreign tax credit in the amount of \$10,195.56 over and above the foreign tax credit claimed in petitioner's return; that petitioner's claim acknowledged that the gross refund claimed for 1942 should be reduced by the amount of \$12.43,

representing an adjustment not in dispute; that petitioner claimed a net refund of \$10,183.13.

(2) For the year 1943 petitioner claimed an additional foreign tax credit in the amount of \$10,862.70 over and above the foreign tax credit claimed in petitioner's return; that petitioner's claim acknowledged that the gross refund claimed for 1943 should be reduced by the amount of \$7.97, representing an adjustment not in dispute; that petitioner claimed a net refund of \$10,854.73.

d. That during the years 1942 and 1943 petitioner, a mutual corporation, was exempt from taxation on its net income from Canadian business under the provisions of the Income War Tax Act, Revised Statutes of Canada of 1927, as amended, Chapter 97, the pertinent provisions of which are as follows:

"Section 4. Incomes not liable to tax.—The following income shall not be liable to taxation hereunder:—

\* \* \*

"(g) Mutual corporations.—The income of mutual corporations not having a capital represented by shares, no part of the income of which inures to the profit of any member thereof, and of life insurance companies except such amount as is credited to shareholders' account;"

e. That for the years 1942 and 1943 the petitioner paid to the Dominion of Canada the fol-

lowing taxes on the net premium income of the petitioner:

(1) For the year 1942 an amount in Canadian funds equivalent to \$15,272.16 United States funds; that said tax was based upon the net premium income of petitioner on its business in Canada; and that for said year the tax rate applicable to the petitioner was 3%;

(2) For the year 1943 an amount in Canadian funds equivalent to \$16,202.54 United States funds; that said tax was based upon the net premium income of the petitioner on its business in Canada; and that for said year the tax rate applicable to the petitioner was 3%.

f. That the petitioner paid the aforementioned taxes to the Dominion of Canada for the years 1942 and 1943 under the provisions of the Special War Revenue Act, Revised Statutes of Canada of 1927, as amended, Chapter 179, the pertinent provisions of which were as follows:

“Section 13. Definitions.—In this Part, unless the context otherwise requires

\* \* \*

“(f) ‘Net premiums’ means, in the case of a company transacting life insurance, the gross premiums received by the company other than the consideration received for annuities, less premiums returned and less the cash value of dividends paid or credited to policyholders; and, in the case of any other company, the gross premiums received or

receivable by the company or paid or payable by the insured less the rebates and return premiums paid on the cancellation of policies: Provided that in the case of a mutual company which carries on business on the premium deposit plan and in the case of an exchange 'net premiums' means the actual net cost of the insurance to the insured during the taxation period together with interest on the excess of the premium deposit over such net cost at the average rate earned by the company on its funds during the said period;—

\* \* \*

“Section 14. Tax on certain insurance companies upon net premiums.—

“1. Every company authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance, other than an association of persons formed on the plan known as Lloyds, a mutual company not carrying on the business of life insurance, and an exchange, shall pay to the Minister a tax of two per centum upon the net premiums received by it in Canada less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1941 and each calendar year thereafter.

“2. Every association of persons formed on the plan known as Lloyds, and every mutual company not carrying on the business of life insurance and not carrying on business on the premium deposit plan, authorized under the laws of the Dominion of



Canada or of any province thereof, to transact the business of insurance, shall pay to the Minister a tax of three per centum upon the net premium received by it in Canada, less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1941 and each calendar year thereafter.

“3. Every mutual company authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance and which carries on business on the premium deposit plan and every exchange so authorized shall pay to the Minister a tax of four per centum upon the net premiums received by it in Canada during the calendar year 1941 and each calendar year thereafter.”

g. That in 1942 the Dominion of Canada amended the aforementioned special War Revenue Act by the enactment of Chapter 32 of the Statutes of 1942 which changed the provisions of said law as follows:

(1) That previous to the enactment of said Chapter 32 all fire insurance companies doing business in the Dominion of Canada were required by said statute to pay to the Dominion of Canada a tax of 1% on their net premium income from their business within the Dominion of Canada;

(2) That in 1942 upon the enactment of said Chapter 32 provision was made for imposing taxes

on all fire insurance companies doing business in Canada; that the basis of said tax was the net premium income of said companies from their business within the Dominion of Canada; that the rates of said tax were as follows:

(a) For all fire insurance companies which were subject to taxation on net income under the Income War Tax Act the rate of 2% on net premium income;

(b) For all fire insurance companies which were not subject to taxation on net income under the Income War Tax Act the rates of 3% and 4% on net premium income.

h. That the petitioner is informed and believes and therefore alleges the following:

(1) That the Dominion of Canada taxes on the net premium income of the petitioner, which were levied under the Special War Revenue Act as amended by Chapter 32 of the statutes of 1942, were levied on fire insurance companies that were exempt from taxes on net income under the Canadian Income War Tax Act;

(2) That the aforementioned taxes were levied by the Dominion of Canada against said insurance companies, including the petitioner, in lieu of a tax upon the income of said insurance companies including the petitioner;

(3) That the aforementioned taxes constitute a "tax paid in lieu of a tax upon income" within the

meaning and intention of Section 131 (h) of the Internal Revenue Code.

i. That the respondent notified petitioner by the letter, IT:90D:FCH, dated July 18, 1947, and statement attached thereto that deficiencies of \$5,-089.03 and \$5,347.81 will be assessed for the years 1942 and 1943, respectively, and in the statement attached to said letter (copy of statement is attached hereto and forms a part of Exhibit A) notified the petitioner that its claims for refunds of \$10,183.13 and \$10,854.73 for the years 1942 and 1943, respectively, would be disallowed by respondent unless the issues involved in the claims for refunds were made a part of a petition to this Court.

Wherefore, the petitioner prays that this Court may hear the proceeding and find that the respondent erred in refusing to allow the petitioner foreign tax credits of \$15,272.16 for the year 1942, and \$16,-202.54 for the year 1943; that the respondent is not justified in asserting deficiencies for the years 1942 and 1943; and that the petitioner is entitled to refunds of over-payments of income taxes in the amounts of \$10,183.13 for the year 1942, and \$10,-854.73 for the year 1943.

/s/ JO D. COOK,

Counsel for Petitioner.

State of Washington,  
County of King—ss.

Alexander Scott, being first duly sworn on oath,

deposes and says: That he is the Treasurer of the above-named petitioner; that he is duly authorized to verify the foregoing petition; that he has read the foregoing petition and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and that those he believes to be true.

/s/ ALEXANDER SCOTT,

Subscribed and sworn to before me this 9th day of October, 1947.

[Seal] /s/ ETHEL I. ELSBURY,  
Notary Public in and for the State of Washington,  
residing at Seattle.

Commission expires Oct. 25, 1951.



## EXHIBIT A

Form 1279

SN-IT-7

Treasury Department  
Internal Revenue Service  
Seattle 1, Washington  
July 18, 1947

Office of  
Internal Revenue Agent in Charge  
Seattle Division  
305 A 1331 Third Avenue Building  
IT:90D:FCH

Northwestern Mutual Fire Association  
217 Pine Street  
Seattle, Washington

Gentlemen:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1942, and December 31, 1943, discloses a deficiency of \$10,436.84, as shown in the statement attached.

In accordance with provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the Tax Court of the United States, at its principal address, Wash-

ington 25, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Seattle 1, Washington, for the attention of IT:90D:FCH. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

GEORGE J. SCHOENEMAN,

Commissioner.

By /s/ L. E. HALLOWELL,

Acting Internal Revenue

Agent in Charge.

FCH:mts

Enclosures:

Statement

Form of Waiver

IT:90D:FCH

## Statement

Northwestern Mutual Fire Association

217 Pine Street

Seattle 1, Washington

Tax liability for the Taxable Years Ended December 31, 1942, and December 31, 1943.

## Income Tax

	Liability	Assessed	Deficiency
Year 1942 .....	\$ 67,163.21	\$ 62,074.18	\$ 5,089.03
Year 1943 .....	70,450.68	65,102.87	5,347.81
Total .....	<u>\$137,613.89</u>	<u>\$127,177.05</u>	<u>\$10,436.84</u>

In making this determination of your income tax liability, careful consideration has been given to the reports of examination dated December 20, 1945; to your protests dated February 15, 1946; to the statements made at the conferences held on May 3, 1946, February 26, 1947, and April 8, 1947; and to your your claims for refund filed on February 28, 1946.

If a petition to The Tax Court of the United States is filed against the deficiencies proposed herein, the issues set forth in your claims for refunds should be made a part of the petition to be considered by The Tax Court in any redetermination of your tax liability. If petitions are not filed, the claims for refunds will be disallowed and official notices will be issued by registered mail in accordance with Section 3772 of the Internal Revenue Code.

The foreign tax credits claimed in your income tax returns for the calendar years 1942 and 1943,

in the respective amounts of \$5,076.60 and \$5,339.84, as income taxes paid to the Dominion of Canada, have been disallowed for the reason that the stated taxes do not constitute "income, war profits or excess profits taxes paid in lieu of a tax upon income, war profits, or excess profits otherwise generally imposed" by Canada. The evidence indicates that the taxes in question were in the nature of an excise imposed under the Special War Revenue Act of Canada and therefore do not meet the requirements of section 131 of the Internal Revenue Code in respect to allowable credits.

For the stated reasons it has been determined also that your claims for refund in the respective amounts of \$10,183.13 and \$10,854.73 should be disallowed for the years 1942 and 1943. The claims for refund are disallowed on the additional ground that a proper application of the provisions of section 131 of the Internal Revenue Code negatives the use of investment income as the basis for computing the limitation factor provided for under subsection (b) thereof, in the case of a mutual insurance company (other than life or marine) paying a tax based upon "the gross amount of income" as defined in section 207 of the Internal Revenue Code.

A copy of this letter and statement has been mailed to your representative, Mr. Jo Dudley Cook, Joseph Vance Building, Seattle 1, Washington, in accordance with the authority contained in the power of attorney executed by you.



## Taxable Year Ended December 31, 1942

## Computation of Net Income

Gross Amount of Net Income Under Section  
207 (a) (2)

Gross income under section 207 (a) (1) and (3), Line 5 of 1942 return.....	\$ 242,971.08
Add: Interest income erroneously reduced by in- terest paid .....	1,242.73
Corrected gross investment income.....	\$ 244,213.81
Net premiums, United States.....	\$7,381,054.65
Net premiums, Canada .....\$ 681,111.30	
Converted at 90.909%.....	619,191.47
	<u>\$8,000,246.12</u>
Less: Dividends to policy-holders:	
United States .....	\$1,347,259.56
Canada \$155,242.77 convert- ed at 90.909%....	141,129.65
	<u>\$1,488,389.21</u>
Interest wholly exempt .....	39,750.00
	<u>1,528,139.21</u>
	<u>\$6,472,106.91</u>
Gross amount of income section 207 (a) (2).....	<u><u>6,716,320.72</u></u>

## Computation of Tax

Under Section 207 (a) (1) and (3)	
Normal tax net income per return.....	\$126,451.85
Tax at 24% on \$126,451.85.....	\$ 30,348.44
Net income, Item 14, Page 1 of return..	\$199,657.79
Less: Dividends received credit.....	41,611.33
Surtax net income .....	<u>\$158,046.46</u>
Surtax at 16% on \$158,046.46.....	25,287.43
Tax under section 207 (a) (1) and (3).....	<u><u>\$ 55,635.87</u></u>
Under Section 207 (a) (2)	
Gross amount of income section 207(a) (2) above	\$6,716,320.72
Tax at 1% on \$6,716,320.72.....	\$ 67,163.21
Tax applicable (greater of tax under section 207 (a) (1) and (3) or section 207 (a) (2)).....	\$ 67,163.21
Tax assessed, Account No. 5-496000.....	62,074.18
Deficiency in tax.....	<u><u>\$ 5,089.03</u></u>

Taxable Year Ended December 31, 1943  
Computation of Net Income

Gross Amount of Income Under Section  
207 (a) (2)

Gross income under section 207 (a)			
(1) and (3), line 5 of 1943 return.....	\$266,722.51		
Add: To correct gross income, add			
amount by which interest re-			
ceived on return was reduced			
by interest paid.....	931.88		
	\$267,654.39		
Deduct: Liquidating dividend received			
which was included in tax-			
able dividends on return....	135.00		
Corrected gross investment income..		\$	267,519.30
Net premiums, United States.....	\$7,758,443.62		
Net premiums, Canada..\$	684,416.33		
Converted at 90.909%.....	622,196.04		
	\$8,380,639.66		
Less: Dividends to policyholders:			
United States .....	\$1,448,978.24		
Canada \$128,382.58			
Converted at			
90.909% .....	116,711.32		
	\$1,565,689.56		
Interest wholly			
exempt .....	37,401.52	1,603,091.08	6,777,548.58
Gross amount of income, section 207 (a) (2).....		\$7,045,067.97	

Computation of Tax  
Under Section 207 (a) (1) and (3)

Normal-tax net income, same as re-		
turn .....	\$	151,828.23
Tax at 24% on \$151,828.23.....	\$	36,438.78
Net income, Item 14, Page 1 of re-		
turn .....	\$	224,927.98
Less: Dividends received		
credit .....		43,899.32
		<hr/>
Surtax net income.....	\$	181,028.66
Tax at 16% on		
\$181,028.66 .....		28,964.59
		<hr/>
	\$	65,403.37
		<hr/> <hr/>

Under Section 207 (a) (2)		
Gross amount of income.....	\$	7,045,067.97
Tax at 1% on \$7,045,067.97.....	\$	70,450.68
Tax assessed, Original Account		
No. 5-496001 .....		65,102.87
		<hr/>
Deficiency in tax.....	\$	5,347.81
		<hr/> <hr/>

Received and filed Oct. 14, 1947, T.C.U.S.

[Title of Tax Court and Cause.]

ANSWER

Now comes the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein, admits and denies as follows:

1. Admits that petitioner is a mutual fire insurance corporation organized and operating under the laws of the State of Washington, and is engaged in business in the United States and in Prov-

inces of Canada, with principal office at 217 Pine Street, Seattle, Washington. Admits that petitioner's Federal income tax returns for the years 1942 and 1943 were filed with the Collector of Internal Revenue, for the District of Washington, at Tacoma, Washington.

2. Admits the allegations contained in paragraph 2 of the petition.

3. a and b. Admits that the taxes in controversy are income taxes for the calendar years 1942 and 1943. Admits that the amounts in dispute are as set forth in subparagraphs a and b of paragraph 3 of the petition.

4. Denies that in determining the deficiencies asserted for the years involved, the respondent committed any errors and specifically denies the allegations of error contained in paragraph 4 of the petition.

5a. (1) and (2). Admits the allegations contained in sub-paragraphs (1) and (2) of paragraph 5a of the petition.

5b. (1) and (2). Admits the allegations contained in sub-paragraphs (1) and (2) of paragraph 5b of the petition.

5c. (1) and (2). Admits that the petitioner filed timely claims for refunds of 1942 and 1943 income taxes based upon the contention that petitioner did not claim the full amount of credit on its original returns for the full amount of the Canadian taxes paid during said years. Admits that the refunds

so claimed by the petitioner for the taxable years 1942 and 1943 are in the respective amounts of \$10,183.13 and \$10,854.73.

5d. Admits that during the years 1942 and 1943 petitioner, a mutual corporation, was exempt from taxation in Canada on its net income from Canadian business under the provisions of the Income War Tax Act, Revised Statutes of Canada of 1927, as amended, Chapter 97, particularly Section 4(g) thereof.

5e. (1) and (2). Admits the allegations contained in subparagraphs (1) and (2) of paragraph 5e of the petition.

5f. Admits that petitioner paid the taxes mentioned in paragraph 5e of its petition to the Dominion of Canada for the years 1942 and 1943 under the provisions of the Special War Revenue Act, Revised Statutes of Canada, 1927, as amended, Chapter 179. For lack of information upon which to base an opinion as to the correctness of the remaining allegations contained in paragraph 5f of the petition, the same are denied.

5g. (1) and (2). Admits that in 1942 the Dominion of Canada amended the Special War Revenue Act by the enactment of new provisions which levied increased taxes upon certain types of fire insurance companies. For lack of information concerning the correctness of the remaining allegations contained in subparagraphs (1) and (2) of paragraph 5g of the petition, the same are denied.



5h. (1), (2) and (3). Denies the allegations contained in subparagraphs (1), (2) and (3) of paragraph 5h of the petition.

5i. Admits that the respondent notified petitioner by letter dated July 18, 1947, and statement attached thereto, that deficiencies of \$5,089.03 and \$5,347.81 were proposed for assessment against it for the years 1942 and 1943, respectively, and in the statement attached to said letter notified petitioner that its claims for refunds of \$10,183.13 and \$10,854.73 for the years 1942 and 1943, respectively, would be disallowed by respondent unless the issues involved in the claims for refunds were made a part of the petition to this Court.

6. Denies generally and specifically each and every material allegation contained in the petition, not hereinbefore specifically admitted, qualified, or denied.

Wherefore, it is prayed that the petitioner's appeal be denied and that the Commissioner's determination of deficiency be approved.

/s/ CHARLES OLIPHANT, WHP.

Chief Counsel, Bureau of  
Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

WILFORD H. PAYNE,  
Special Attorney,  
Bureau of Internal Revenue.

Received and filed Nov. 20, 1947, T.C.U.S.

[Title of Tax Court and Cause.]

### STIPULATION

It Is Hereby Stipulated and Agreed by and between the parties to the above-entitled action as follows:

1. That the Petitioner is a mutual fire insurance corporation organized and operating under the laws of the State of Washington, and is duly authorized, and engaged in the business of writing insurance against the perils of fire and allied lines in all states of the United States and in Canada, with its principal office at 217 Pine Street, Seattle, Washington; that income tax returns for the periods involved in the above-entitled action were filed with the Collector of Internal Revenue for the District of Washington, at Tacoma, Washington, within and under extensions of time allowed by the Commissioner.

2. That the notice of deficiency with statement attached (a copy of which is attached to the Petition herein) was mailed to the Petitioner on July 18, 1947.

3. That the taxes in controversy are income taxes for the calendar years 1942 and 1943 and the amounts in dispute are as follows:

a. For the year 1942 the Commissioner asserts a deficiency of \$5,089.03; whereas for said year Petitioner claims a refund of \$10,183.13;

b. For the year 1943 the Commissioner asserts a deficiency of \$5,347.81; whereas for said year Petitioner claims a refund of \$10,854.73.

4. That Petitioner made a timely filing of 1942 and 1943 income tax returns on Form 1120 M under extensions granted by the Commissioner; that said returns were made on the accrual basis; that Petitioner made a timely payment of Petitioner's tax due in accordance with the calculations in Petitioner's returns for each of the years 1942 and 1943 as hereinafter set forth, and that in said returns foreign tax credits were claimed as hereinafter set forth:

a. For the year 1942 Petitioner made timely payment of the full amount of Petitioner's tax due in accordance with the calculations in Petitioner's original return for the year 1942; that said tax was paid in instalments in the following amounts as set forth below:

March 15, 1943.....	\$17,500.00	
June 11, 1943.....	13,537.10	
	<hr/>	\$31,037.10
September 14, 1943.....	\$15,518.54	
December 14, 1943.....	15,518.54	
	<hr/>	31,037.08
		<hr/>
		\$62,074.18

b. For the year 1943 Petitioner made timely payment of the full amount of Petitioner's tax due in accordance with the calculations in Petitioner's original return for the year 1943; that said tax was

paid in instalments in the following amounts as set forth below:

March 15, 1944.....	\$17,500.00	
June 15, 1944.....	15,051.44	
	<hr/>	\$32,551.44
September 14, 1944.....	\$16,275.72	
December 13, 1944.....	16,275.71	
	<hr/>	32,551.43
		<hr/>
		\$65,102.87

c. For the taxable year 1942 a foreign tax credit of \$5,076.60 was claimed;

d. For the taxable year 1943 a foreign tax credit of \$5,339.84 was claimed;

e. That upon audit of Petitioner's tax returns for 1942 and 1943 the Petitioner's tax without deduction for foreign tax credit was established at:

(1) \$67,163.21 for the year 1942;

(2) \$70,450.68 for the year 1943.

5. That Petitioner filed timely claims for refunds for 1942 and 1943 income taxes paid, which were made on the basis that Petitioner did not claim credit on Petitioner's original returns for the full amount of Canadian taxes paid by Petitioner during said periods; and further Petitioner claims to have made an error in the calculation of the foreign tax credit; that Petitioner's claims for refunds were as follows:

a. For the year 1942 Petitioner claimed an additional foreign tax credit in the amount of \$10,195.56 over and above the foreign tax credit claimed in Petitioner's return; that Petitioner's claim acknowledged that the gross refund claimed for 1942 should be reduced by the amount of \$12.43, representing an adjustment not in dispute; that Petitioner claimed a net refund of \$10,183.13;

b. For the year 1943 Petitioner claimed an additional foreign tax credit in the amount of \$10,862.70 over and above the foreign tax credit claimed in Petitioner's return; that Petitioner's claim acknowledge that the gross refund claimed for 1943 should be reduced by the amount of \$7.97, representing an adjustment not in dispute; that Petitioner claimed a net refund of \$10,854.73.

6. For the tax years 1942 and 1943 the Petitioner's normal-tax net income for the purpose of the tax return Form 1120 M, Line 19, Page 1, from all sources, and the portion thereof from sources in the Dominion of Canada (converted to U. S. funds) were as follows:

a. For the year 1942:

(1) From all sources \$126,451.85;

(2) From sources in the Dominion of Canada (converted to U. S. funds) \$37,843.46.

b. For the year 1943:

(1) From all sources \$151,828.23;



(2) From sources in the Dominion of Canada (converted to U. S. funds) \$40,943.06.

7. For the taxable years 1942 and 1943 the Petitioner's gross amount of income from all sources, and its gross amount of income from sources in the Dominion of Canada (converted to U. S. funds) was as follows:

a. For the year 1942:

(1) Petitioner's gross amount of income from all sources was \$6,716,320.72;

(2) Petitioner's gross amount of income from sources in the Dominion of Canada (converted to U. S. funds) was \$507,681.54.

b. For the year 1943:

(1) Petitioner's gross amount of income from all sources was \$7,045,067.97;

(2) Petitioner's gross amount of income from sources in the Dominion of Canada (converted to U. S. funds) was \$533,987.07.

8. That during the years 1942 and 1943 Petitioner, a mutual fire insurance corporation, was not liable to tax on its net income from Canadian business under the provisions of the Canadian Income War Tax Act of 1917, as amended by Chapter 97, the provisions of which are set forth in the Revised Statutes of Canada of 1927, the pertinent provisions of which are as follows:

“Section 4. Incomes not liable to tax.—The following income shall not be liable to taxation hereunder:—

\* \* \*

“(g) Mutual corporations.—The income of mutual corporations not having a capital represented by shares, no part of the income of which inures to the profit of any member thereof, and of life insurance companies except such amount as is credited to shareholders’ account;”

9. That for the years 1942 and 1943 the Petitioner paid to the Dominion of Canada the following taxes on the “net premiums” of the Petitioner:

a. For the year 1942 an amount in Canadian funds equivalent to \$15,272.16 United States funds; that said tax was based upon the “net premiums” of Petitioner on its business in Canada; and that for said year the tax rate applicable to the Petitioner was 3%;

b. For the year 1943 an amount in Canadian funds equivalent to \$16,202.54 United States funds; that said tax was based upon the “net premiums” of the Petitioner on its business in Canada; and that for said year the tax rate applicable to the Petitioner was 3%.

10. That the Petitioner paid the aforementioned taxes to the Dominion of Canada for the years 1942 and 1943 under the provisions of the Special War Revenue Act originally enacted in 1915, con-

tained in the Revised Statutes of Canada of 1927, as amended in 1942 by Chapter 32 of the Special War Revenue Act, Part III, the pertinent provisions of which are as follows:

“Section 13. Definitions.—In this Part, unless the context otherwise requires

\* \* \*

“(f) ‘Net premiums’ means, in the case of a company transacting life insurance, the gross premiums received by the company other than the consideration received for annuities, less premiums returned and less the cash value of dividends paid or credited to policyholders; and, in the case of any other company, the gross premiums received or receivable by the company or paid or payable by the insured less the rebates and return premiums paid on the cancellation of policies; Provided that in the case of a mutual company which carries on business on the premium deposit plan and in the case of an exchange ‘net premiums’ means the actual net cost of the insurance to the insured during the taxation period together with interest on the excess of the premium deposit over such net cost at the average rate earned by the company on its funds during the said period;—

\* \* \*

“Section 14. Tax on certain insurance companies upon net premiums.—

“1. Every company authorized under the laws of the Dominion of Canada or of any province thereof,

to transact the business of insurance, other than an association of persons formed on the plan known as Lloyds, a mutual company not carrying on the business of life insurance, and an exchange, shall pay to the Minister a tax of two per centum upon the net premiums received by it in Canada less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1941 and each calendar year thereafter.

“2. Every association of persons formed on the plan known as Lloyds, and every mutual company not carrying on the business of life insurance and not carrying on business on the premium deposit plan, authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance, shall pay to the Minister a tax of three per centum upon the net premiums received by it in Canada, less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1941 and each calendar year thereafter.

“3. Every mutual company authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance and which carries on business on the premium deposit plan and every exchange so authorized shall pay to the Minister a tax of four per centum upon the net premiums received by it in Canada during the calendar year 1941 and each calendar year thereafter.”

11. That in 1942 the Dominion of Canada amended the aforementioned Special War Revenue Act of 1915 by the enactment of Chapter 32 of the Statutes of 1942, and that said amendment changed the provisions of the Special War Revenue Act:

a. Previous to the enactment of said amendment all fire insurance companies doing business in the Dominion of Canada, including this Petitioner, were required by the provisions of the Special War Revenue Act to pay to the Dominion of Canada a tax of 1% on their net premiums from their business within the Dominion of Canada in accordance with the following provision of said law:

(Special War Revenue Act of Canada of 1915, Chapter 179, Part 3, Section 14.)

“Section 14. Every company, licensed or registered or otherwise authorized to transact in Canada or in any province thereof, the business of insurance shall pay to the Minister a tax of one per cent upon the net premiums received by it in Canada on and after the first day of January in any year.”

b. Upon the enactment of said Chapter 32 of the Statutes of 1942, provision was made for increasing the net premium tax on all fire insurance companies doing business in Canada, including this Petitioner, and that the basis for said tax was the “net premiums” of said companies from their business within the Dominion of Canada (See Special War Revenue Act of 1915 as amended to date; con-



tained in Chapter 179, R. S. 1927; Chapter 32, Laws of 1942, Part III, Sections 13 and 14, the pertinent provisions of which are quoted at length in Paragraph 10 hereof):

(1) For all fire insurance companies which were subject by Canadian law to taxation on their net income under the Income War Tax Act of 1917 (which did not include this Petitioner) the Special War Revenue Act of 1915, as amended by Chapter 32 of the Statutes of 1942, imposed a tax at the rate of 2% on their "net premiums" as follows:

"Section 14. 1. Every company authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance, other than an association of persons formed on the plan known as Lloyds, a mutual company not carrying on the business of life insurance and an exchange, shall pay to the Minister a tax of two per centum upon the net premiums received by it in Canada less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1941 and each calendar year thereafter."

(2) For all mutual fire insurance companies, including the Petitioner herein, not subject to taxation on their net income under the provisions of the Canadian Income War Tax Act of 1917 (See Income War Tax Act of 1917 contained in Revised Statutes of Canada of 1927 as amended by Chapter 97, Section 4, subsection (g), the pertinent pro-

visions of which are quoted in Paragraph 8 hereof), the Special War Revenue Act of 1915, as amended by Chapter 32 of the Statutes of 1942, imposed a tax at the rates of 3% and 4% on the "net premiums" as follows:

"Section 14. 2. Every association of persons formed on the plan known as Lloyds, and every mutual company not carrying on the business of life insurance and not carrying on business on the premium deposit plan, authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance, shall pay to the Minister a tax of three per centum upon the net premiums received by it in Canada, less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1941 and each calendar year thereafter.

"Section 14. 3. Every mutual company authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance and which carries on business on the premium deposit plan and every exchange so authorized shall pay to the Minister a tax of four per centum upon the net premiums received by it in Canada during the calendar year 1941 and each calendar year thereafter."

12. That in the Dominion of Canada the Special War Revenue Act of 1915 and the Income War Tax Act of 1917 are administered as follows:

a. The taxes on insurance companies levied

under the Special War Revenue Act of 1915, Chapter 179, as contained in Revised Statutes of Canada of 1927, as amended, are payable to the Minister of Finance:

(1) The administrative details of collection and audit of taxes payable by insurance companies under the Special War Revenue Act of 1915, as amended, are handled by the Department of Insurance;

(2) Taxes other than taxes on insurance companies payable under the Special War Revenue Act of 1915, as amended, are handled as to the details of collection and audit by the Department of National Revenue.

b. The income taxes levied under the Canadian Income War Tax Act of 1917, Chapter 97, contained in Revised Statutes of Canada of 1927, as amended, are payable to the Minister of National Revenue:

(1) The general administration and the auditing of returns for taxpayers, other than insurance companies, under the Income War Tax Act is handled by the Department of National Revenue;

(2) The auditing of the income tax returns of insurance companies which are subject to the provisions of the Income War Tax Act is handled by the Department of Insurance.

13. The Income War Tax Act of Canada originally enacted in 1917 was amended in 1946 so that mutual fire insurance companies such as the Peti-

tioner (excepting only those mutual fire insurance companies deriving their premiums wholly from the insurance of churches, schools, or other religious, educational or charitable institutions) were made subject to the general income tax law of Canada (See Canadian Income War Tax Act of 1917, Chapter 28; contained in Revised Statutes of Canada of 1927, Chapter 97, as amended by Part I, Section 3, which defines taxable income as follows:

“Section 3. “Income”.—1. For the purposes of this Act, “income” means the annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary, or other fixed amount, or unascertained as being fees or emoluments, or as being profits from a trade or commercial or financial or other business or calling, directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be whether derived from sources within Canada or elsewhere; and shall include the interest, dividends or profits directly or indirectly received from money at interest upon any security or without security, or from stocks, or from any other investment, and, whether such gains or profits are divided or distributed or not, and also the annual profit or gain from any other source——.”

and Part II, Section 4, subparagraph (g), which defines excepted incomes as follows:

“Section 4. Incomes not liable to tax.—The fol-



lowing income shall not be liable to taxation hereunder:—

\* \* \*

“(g) Mutual corporations.—The income of mutual corporations not having a capital represented by shares, no part of the income of which inures to the benefit of any member thereof, except mutual insurance corporations that do not derive their premiums wholly from the insurance of churches, schools or other religious, educational or charitable institutions——”).

Prior to the enactment in 1946 of the above amendment to the Income War Tax Act of 1917 mutual fire insurance companies, such as the Petitioner, were not liable to tax under the provisions of Section 4, subsection (g) of the Income War Tax Act of 1917 (See Income War Tax Act of 1917, Section 4, subsection (g), the pertinent provisions of which are quoted in Paragraph 8 hereof).

14. That in 1946 at the time of the enactment of the amendment to the Income War Tax Act of 1917, the provisions of which are referred to in Paragraph 13 hereof, the Special War Revenue Act (the net premium tax), as amended in 1942, was changed as follows: (See Special War Revenue Act of 1915, as amended by Chapter 32, Section 14, subsection (2), Statutes of 1942; and Special War



Revenue Act of 1915, as amended by Chapter 65, Section 14, subsection (1), Statutes of 1946).

a. That the rate of said tax on mutual fire insurance companies, such as the Petitioner, was 3% on "net premiums" under the 1942 amendment and prior to the 1946 amendment referred to herein (See Special War Revenue Act of 1915, as amended by Chapter 32, Section 14, subsection (2) Statutes of 1942, the pertinent provisions of which are quoted in Paragraph 10 hereof).

b. That upon the enactment of the 1946 amendment referred to herein, the rate of said tax on mutual fire insurance companies, such as the Petitioner, was reduced from 3% to 2% (See Special War Revenue Act of 1915, as amended by Chapter 65, Laws of 1946, Section 14, subparagraph (1), which reads as follows:

"Section 14. 1. Every company authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance, other than an association of persons formed on the plan known as Lloyds, and an exchange, shall pay to the Minister a tax of two per centum upon the net premiums received by it in Canada less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1947 and each calendar year thereafter.")

c. The 1946 amendments to the Special War

Revenue Act also changed the name of the Act to the "Canadian Excise Tax Act."

15. That at the time of the amendment of Section 131 of the United States Internal Revenue Code in 1942, the Committee on Finance of the Senate had this to say concerning subsection (h) of Section 131:

"Your committee believes further amendments should be made in section 131. Under that section as it now stands, a credit is allowed against United States Tax for income, war profits, or excess profits taxes paid or accrued to any foreign country or to any possession of the United States. In the interpretation of the term 'income tax', the Commissioner, the Board, and the Courts have consistently adhered to a concept of income tax rather closely related to our own, and if such foreign tax was not imposed upon a basis corresponding approximately to net income it was not recognized as a basis for such credit. Thus, if a foreign country in imposing income taxation authorized, for reasons growing out of the administrative difficulties of determining net income or taxable basis within that country, a United States domestic corporation doing business in such country to pay a tax in lieu of such income tax but measured, for example, by gross income, gross sales or a number of units produced within the country, such tax has not heretofore been recognized as a basis for credit. Your committee has deemed it desirable to extend the scope of this

section. Accordingly, subsection (f) of section 160 provides that the term 'income, war profits, and excess profits taxes' shall, for the purpose of sections 131 and 23(c)(1), include a tax paid by a domestic taxpayer in lieu of the tax upon income, war profits, and excess profits taxes which would otherwise be imposed upon such taxpayer by any foreign country or by any possession of the United States. The limitation upon the amount of the credit will, of course, continue to apply, so that it will be allowed only if and to the extent the taxpayer has net income from sources within the foreign country or from sources without the United States, as the case may be."

16. That the Respondent notified the Petitioner by letter IT:90D:FCH, dated July 18, 1947, and statement attached thereto, that deficiencies of \$5,089.03 and \$5,347.81 were proposed for assessment for the years 1942 and 1943 respectively, and in the statement attached to said letter (a copy of said statement being attached to the Petition), notified the Petitioner that its claims for refunds of \$10,183.13 and \$10,854.73 for the years 1942 and 1943 respectively would be disallowed by Respondent unless the issues involved in the claims for refunds were made a part of the petition to this Court.

17. That the Petitioner and the Respondent have agreed to offer in evidence the following original documents with the request that they be marked

as joint Exhibits as set forth herein, and with the request that the Court shall accept said original documents in evidence in this case but will permit the original documents to be withdrawn and photostatic copies of the same substituted therefor at such time as said photostatic copies may become available:

a. For the calendar year 1942 the following documents:

(1) Petitioner's Income Tax Return for the calendar year 1942 on Form 1120 M, Mutual Fire Insurance Company Tax Return, marked Exhibit 1 A;

2. Petitioner's statement in support of foreign tax credit claimed on Form 1118, which was attached to Petitioner's 1942 Income Tax Return, marked Exhibit 2 B;

3. Petitioner's claim for refund of 1942 taxes paid, as filed by Petitioner on Form 843, and certification of tax payments by the Collector on the reverse side of said form, marked Exhibit 3 C;

(4) Petitioner's statement in support of foreign tax credit claimed on Form 1118, which was attached to Petitioner's claim for refund of 1942 taxes paid, marked Exhibit 4 D;

(5) A copy of Petitioner's tax return made to the Dominion of Canada, showing taxes paid by Petitioner for 1942 under the Special War Revenue Act, marked Exhibit 5 E.

b. For the calendar year 1943 the following documents:

(1) Petitioner's Income Tax Return for the calendar year 1943 on Form 1120 M, Mutual Fire Insurance Company Tax Return, marked Exhibit 6 F;

(2) Petitioner's statement in support of foreign tax credit claimed on Form 1118, which was attached to Petitioner's 1943 Income Tax Return, marked Exhibit 7 G;

(3) Petitioner's claim for refund of 1943 taxes paid, as filed by Petitioner on Form 843; and certification of tax payments by the Collector on the reverse side of said form, marked Exhibit 8 H;

(4) Petitioner's statement in support of foreign tax credit claimed on Form 1118, which was attached to Petitioner's claim for refund of 1943 taxes paid, marked Exhibit 9 I;

(5) A copy of Petitioner's tax return made to the Dominion of Canada, showing taxes paid by Petitioner for 1943 under the Special War Revenue Act, marked Exhibit 10 J.

Dated at Seattle, Washington, this 17th day of May, 1948.

/s/ JO D. COOK,

Attorney for Petitioner.

/s/ CHARLES OLIPHANT,

W.H.P.

Attorney for Respondent.

Filed May 17, 1948 T.C.U.S.



Before the Tax Court of the United States

Docket No. 16147

NORTHWESTERN MUTUAL FIRE ASSOCIATION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

Before: Honorable Eugene Black,  
Judge.

#### APPEARANCES

JO D. COOK, ESQ.,  
appearing on behalf of the Petitioner.

WILFORD H. PAYNE, ESQ.,  
appearing on behalf of the Commissioner  
of Internal Revenue,  
Respondent.

#### PROCEEDINGS

The Court: The Clerk will call the next case.

The Clerk: Docket No. 16147, Northwestern  
Mutual Fire Association.

Mr. Payne: Wilford H. Payne, for the Respondent.

Mr. Cook: Jo D. Cook, for the Petitioner.

The Court: You may proceed.

## Opening Statement on Behalf of the Petitioner

By Mr. Cook

Mr. Cook: Your Honor, the issues, are two issues in this matter. All the facts necessary for a decision have been stipulated. The question involves the right of the Petitioner to a credit for foreign taxes to the Dominion of Canada, and if they are entitled to that credit, the amount is stipulated. I have here, in duplicate form the stipulation, covering all the necessary facts which I should request leave to file at this time.

The Court: Very well, the stipulation of facts will be received as evidence in the case. Do you have anything else?

Mr. Cook: We have certain exhibits. I would like to have received in evidence the exhibits which are referred to in Paragraph 17 of the stipulation, and it is understood that that they come from the Respondent's files and are to be returned to the Respondent upon substitution of photostatic copies.

The Court: Well, that understanding will be noted.

Mr. Cook: Mr. Payne is more familiar with the procedure, and I will ask that he take care of the matter of the receipt in evidence of the exhibits.

Mr. Payne: The parties offer at this time, pursuant to 17-A-1 of the stipulation, the income tax return of the Petitioner for the year 1942, to be marked, pursuant to our stipulation, as Joint Exhibit 1-A.

The Court: It will be received as Joint Exhibit 1-A.

(The document referred to was marked and received in evidence as Joint Exhibit 1-A.)

Mr. Payne: We also offer at this time, in accordance with Paragraph 17-A-2 of the stipulation, the Petitioner's statement in support of foreign tax credits on Form 1118, to be marked as Joint Exhibit No. 2.

The Court: It will be received in evidence and marked as Joint Exhibit No. 2.

(The document referred to was marked and received in evidence as Joint Exhibit 2-B.)

Mr. Payne: In accordance with Paragraph 17-A-3 of the stipulation, a claim for refund for the year 1942, which we ask be marked as Joint Exhibit 3-C.

The Court: It will be received as Joint Exhibit 3-C.

(The document referred to was marked and received in evidence as Joint Exhibit 3-C.)

Mr. Payne: In accordance with Paragraph 17-A-4 of the stipulation, in evidence, we offer Petitioner's statement in support of foreign tax credit on Form 1118, which was attached to its claim for refund, just introduced. We offer this as Joint Exhibit 4-D.

The Court: It will be received as Joint Exhibit 4-D.

(The document referred to was marked and received in evidence as Joint Exhibit 4-D.)

Mr. Payne: In accordance with Paragraph 17-A-5 of the stipulation, the parties offer the Petitioner's tax return made to the Dominion of Canada, identified in the stipulation as Joint Exhibit 5-E.

The Court: It will be received as Joint Exhibit 5-E.

(The document referred to was marked and received in evidence as Joint Exhibit 5-E.)

Mr. Payne: Now, coming to Paragraph 17-B-1 of the stipulation, the Petitioner's income tax return for the year 1943, we offer that as Joint Exhibit 6-F.

The Court: It will be received and marked as Exhibit 6-F.

(The document referred to was marked and received in evidence as Joint Exhibit 6-F.)

Mr. Payne: In accordance with Paragraph 17-B-2 of the stipulation, we offer the statement in support of foreign tax credit on Form 1118, which we will ask be marked as Joint Exhibit 7-G.

The Court: It will be received as Joint Exhibit 7-G.

(The document referred to was marked and received in evidence as Joint Exhibit 7-G.)

Mr. Payne: We offer a document identified in Paragraph 17-B-3 of the stipulation as Joint Ex-

hibit 8-H, which is a claim for refund for the year 1943.

The Court: It will be received as Joint Exhibit 8-H.

(The document referred to was marked and received in evidence as Joint Exhibit 8-H.)

Mr. Payne: The parties offer at this time, a document identified in Paragraph 17-B-4 of the stipulation as Joint Exhibit 9-I.

The Court: It will be received in evidence as Joint Exhibit 9-I.

(The document referred to was marked and received in evidence as Joint Exhibit 9-I.)

Mr. Payne: The parties offer a document identified in Paragraph 17-B-5 of the stipulation as Joint Exhibit 10-J.

The Court: It will be received as Joint Exhibit 10-J.

(The document referred to was marked and received in evidence as Joint Exhibit 10-J.)

The Court: Now, you desire to file briefs simultaneously under the terms granted under the rules?

Mr. Payne: That would be satisfactory.

The Court: That will be July 5 for the briefs, allowing the full 45 days.

Mr. Cook: July 5?

The Court: Yes. And then thereafter you may file a reply brief, if you care to do so, on July 25.

Mr. Payne: That is agreeable.

Mr. Cook: Very, well, your Honor.



(Whereupon, at 11:20 a.m., May 17, 1948, the case was concluded.)

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[Title of Tax Court and Cause.]

Promulgated March 30, 1949.

The petitioner, a domestic mutual fire insurance company doing business in Canada, paid taxes in 1942 and 1943 to Canada measured by the net premiums received in Canada, less premiums paid for reinsurance, in accordance with the provisions of the Canadian Special War Revenue Act of 1915, as amended. Held, the taxes paid upon the net premiums were not taxes "in lieu of a tax upon income" as those terms are used in section 131(h), I.R.C. and petitioner is not entitled to a credit for income taxes paid to a foreign government under section 131, I.R.C.

Jo D. Cook, Esq., for the petitioner.

Wilford H. Payne, Esq., for the respondent.

### OPINION

Black, Judge:

This proceeding involves deficiencies in petitioner's income taxes for the years 1942 and 1943 in the respective amounts of \$5,089.03 and \$5,347.81. The petitioner claims refunds for the years 1942 and 1943 in the respective amounts of \$10,183.13 and \$10,854.73.

The deficiencies are due primarily to the disallowance of foreign tax credits claimed in the petition-

er's income tax returns for the calendar years 1942 and 1943 in the respective amounts of \$5,076.60 and \$5,339.84 as income taxes paid to the Dominion of Canada. The respondent in the deficiency notice explained this disallowance as follows:

The foreign tax credits claimed in your income tax returns for the calendar years 1942 and 1943, in the respective amounts of \$5,076.60 and \$5,339.84, as income taxes paid to the Dominion of Canada, have been disallowed for the reason that the stated taxes do not constitute "income, war profits or excess profits taxes paid in lieu of a tax upon income, war profits, or excess profits otherwise generally imposed" by Canada. The evidence indicates that the taxes in question were in the nature of an excise imposed under the Special War Revenue Act of Canada and therefore do not meet the requirements of section 131 of the Internal Revenue Code in respect to allowable credits.

For the stated reasons it has been determined also that your claims for refund in the respective amounts of \$10,183.13 and \$10,854.73 should be disallowed for the years 1942 and 1943. The claims for refund are disallowed on the additional ground that a proper application of the provisions of section 131 of the Internal Revenue Code negatives the use of investment income as the basis for computing the limitation factor provided for under subsection (b) thereof, in the case of a mutual insurance company (other than life or marine) paying a tax based upon "the gross amount of income"

as defined in section 207 of the Internal Revenue Code.

The petitioner by appropriate assignments of error contests these adjustments and claims refunds.

The case was submitted upon a stipulation of facts and joint exhibits which are adopted as our findings of fact. They may be summarized as follows:

The petitioner is a mutual fire insurance corporation organized and operating under the laws of the State of Washington, and is duly authorized and engaged in the business of writing insurance against the perils of fire and allied lines in all states of the United States and in Canada, with its principal office in Seattle, Washington. Its income tax returns for the years 1942 and 1943 were prepared on the accrual basis and were filed with the collector of internal revenue for the district of Washington at Tacoma, Washington within and under extensions of time allowed by the Commissioner.

In the years 1942 and 1943 the petitioner paid to the Dominion of Canada amounts in Canadian funds equivalent to \$15,272.16 and \$16,202.54, respectively, in United States funds in taxes in accordance with the provisions of the Canadian Special War Revenue Act of 1915, as amended in 1942.<sup>1</sup> The said tax was based upon the "net premiums" of petitioner on its business in Canada and for said years the tax rate applicable to petitioner was three per cent.

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<sup>1</sup>Special War Revenue Act of 1915 contained in the Revised Statutes of Canada of 1927, as amended

In petitioner's returns for the years 1942 and 1943 it claimed foreign tax credits in the respective amounts of \$5,076.60 and \$5,339.84.

The petitioner's gross amount of income for the years 1942 and 1943 from all sources was \$6,716,320.72 and \$7,045,067.97, respectively, and its gross amount of income from sources in the Dominion of Canada (converted to United States funds) was \$507,681.54 and \$533,987.07, respectively.

In the years 1942 and 1943 the petitioner's nor-

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in 1942 by Chapter 32 of the Special War Revenue Act, Part III.

Section 13. Definitions.—In this Part, unless the context otherwise requires

\* \* \*

(f) "Net premiums" means, in the case of a company transacting life insurance, the gross premiums received by the company other than the consideration received for annuities, less premiums returned and less the cash value of dividends paid or credited to policyholders; and, in the case of any other company, the gross premiums received or receivable by the company or paid or payable by the insured less the rebates and return premiums paid on the cancellation of policies; provided that in the case of a mutual company which carries on business on the premium deposit plan and in the case of an exchange "net premiums" means the actual net cost of the insurance to the insured during the taxation period together with interest on the excess of the premium deposit over such net cost at the average rate earned by the company on its funds during the said period;—

\* \* \*

Section 14. Tax on certain insurance companies upon net premiums.—

1. Every company authorized under the laws of



mal tax net income from all sources was \$126,451.85 and \$151,828.23, respectively, while for said years petitioner's normal tax net income from sources in the Dominion of Canada (converted to United States funds) was \$37,843.46 and \$40,943.06, respectively.

During the years 1942 and 1943 petitioner was not liable to tax on its net income from Canadian

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the Dominion of Canada or of any province thereof, to transact the business of insurance, other than an association of persons formed on the plan known as Lloyds, a mutual company not carrying on the business of life insurance, and an exchange, shall pay to the Minister a tax of two per centum upon the net premiums received by it in Canada less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1941 and each calendar year thereafter.

2. Every association of persons formed on the plan known as Lloyds, and every mutual company not carrying on the business of life insurance and not carrying on business on the premium deposit plan, authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance, shall pay to the Minister a tax of three per centum upon the net premiums received by it in Canada, less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1941 and each calendar year thereafter.

3. Every mutual company authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance and which carries on business on the premium deposit plan and every exchange so authorized shall pay to the Minister a tax of four per centum upon the net premiums received by it in Canada during the calendar year 1941 and each calendar year thereafter.



business under the provisions of the Canadian Income War Tax Act of 1917, as amended by chapter 97, the provisions of which are set forth in the revised Statutes of Canada of 1927.<sup>2</sup>

Prior to the year 1942 the petitioner was required by the provisions of the Special War Revenue Act of 1915 to pay to the Dominion of Canada a tax of one per cent on its net premiums from its business within the Dominion of Canada.<sup>3</sup>

In 1942 the Dominion of Canada amended the Special War Revenue Act of 1915 by the enactment of chapter 32 of the Statutes of 1942, heretofore set out, increasing the net premium tax on all fire insurance companies doing business in Canada, including the petitioner and the basis for said tax was the "net premiums" of said companies from their business within the Dominion of Canada. For

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<sup>2</sup>Section 4. Incomes not liable to tax.—The following income shall not be liable to taxation hereunder:—

\* \* \*

(g) Mutual corporations.—The income of mutual corporations not having a capital represented by shares, no part of the income of which inures to the profit of any member thereof, and of life insurance companies except such amount as is credited to shareholders' account; \* \* \*

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<sup>3</sup>Special War Revenue Act of 1915, Chapter 179  
Part 3.

Section 14. Every company, licensed or registered or otherwise authorized to transact in Canada or in any province thereof, the business of insurance shall pay to the Minister a tax of one per cent upon the net premiums received by it in Canada on and after the first day of January in any year.

all mutual fire insurance companies such as the petitioner, not subject to taxation on their net income under the provisions of the Canadian Income War Tax Act of 1917, the rate was increased from one to three per cent. For all fire insurance companies which were subject by Canadian law to taxation on their net income under the Income War Tax Act of 1917 (which did not include this petitioner) the rate was increased from one to two per cent.

In the year 1946 the Canadian revenue measures were revised and the Income War Tax Act originally enacted in 1917 was amended so that mutual fire insurance companies such as petitioner (excepting only those mutual fire insurance companies deriving their premiums wholly from the insurance of churches, schools, or other religious, educational or charitable institutions) were made subject to the general income tax law of Canada.<sup>4</sup> Prior to the enactment in 1946 of the above amendment to

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<sup>4</sup>Canadian Income War Tax Act of 1917, chapter 28, contained in the Revised Statutes of Canada of 1927, chapter 97, as amended by Part I, Section 3 and Part II, Section 4.

Part I, Section 3. "Income."—1. For the purposes of this Act, "income" means the annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary, or other fixed amount, or unascertained as being fees or emoluments, or as being profits from a trade or commercial or financial or other business or calling, directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be whether derived from

the Income War Tax Act of 1917, mutual fire insurance companies such as petitioner were not liable to tax under the provisions of the Income War Tax Act of 1917 as hereinabove set out.

Concurrent with the above change in the Income War Tax Act of 1917 the Special War Revenue Act of 1915, as amended in 1942, was amended further changing the name of the act from "Special War Revenue Act" to the "Canadian Excise Tax Act," and said amendment further provided that the rate of tax upon the net premiums for mutual fire insurance companies, such as petitioner, should be reduced from three per cent to two per cent.<sup>5</sup>

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<sup>5</sup>Special War Revenue Act of 1915, as amended by chapter 65, Laws of 1946, Section 14.

Section 14. 1. Every company authorized under the laws of the Dominion of Canada or of any province thereof, to transact the business of insurance, other than an association of persons formed on the plan known as Lloyds, and an exchange, shall pay to the Minister a tax of two per centum upon the net premiums received by it in Canada less net premiums paid for reinsurance to companies or associations to which this section applies, during the year 1947 and each calendar year thereafter.

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sources within Canada or elsewhere; and shall include the interest, dividends or profits directly or indirectly received from money at interest upon any security or without security, or from stocks, or from any other investment, and, whether such gains or profits are divided or distributed or not, and also the annual profit or gain from any other source.

\* \* \*

Part II, Section 4. Incomes not liable to tax.—

In 1942 and 1943 the taxes imposed under the Special War Revenue Act of 1915, as amended, and the Income War Tax Act of 1917, as amended, were paid to the Minister of National Revenue, sometimes referred to as the Minister of Finance.

In the years 1942 and 1943 the administrative details of collection and auditing of taxes payable by insurance companies under the Special War Revenue Act of 1915, as amended, and the auditing of income tax returns of insurance companies which were subject to the provisions of the Income War Tax Act, as amended, were handled by the Department of Insurance.

In the years 1942 and 1943 the details of collection and auditing of taxes other than taxes on insurance companies payable under the Special War Revenue Act of 1915, as amended, and the general administration and the auditing of returns of taxpayers other than insurance companies under the Income War Tax Act of 1917 were handled by the Department of National Revenue.

In its returns for the years 1942 and 1943 and

---

The following income shall not be liable to taxation hereunder:—

\* \* \*

(g) Mutual corporations.—The income of mutual corporations not having a capital represented by shares, no part of the income of which inures to the benefit of any member thereof, except mutual insurance corporations that do not derive their premiums wholly from the insurance of churches, schools or other religious, educational or charitable institutions \* \* \*.



in The Statement in Support of Credit for the Foreign Tax Paid (Form 1118) for said years, petitioner computed the amount of credit on the gross amount of income for each year which constituted its taxable income and formed the basis under the statute for determining the amount of tax due in this country. On such basis and using the ratio of the total gross income from Canada (\$507,681.54 for 1942 and \$533,987.07 for 1943), to total gross income in its returns from all sources for those years (\$6,715,077.99 for 1942 and \$7,044,271.09 for 1943) the amounts of the credits so computed were \$5,076.60 and \$5,339.84 for the years 1942 and 1943, respectively. These claimed credits were disallowed by respondent in the deficiency notice.

In its claims for refunds for 1942 and 1943 and The Statements in Support of Credit for Foreign Taxes which were attached thereto, petitioner claimed that the credit for each year should be computed and determined upon the basis which the ratio of the "normal tax net income" from sources in Canada bears to the "normal tax net income" from all sources, i.e., in the ratio which the "normal tax net income" of \$37,843.46 from Canadian sources bears to the "normal tax net income" of \$126,451.85 from all sources for the year 1942; and in the ratio which the "normal tax net income" of \$40,943.06 from Canadian sources bears to "normal tax net income" of \$151,828.23 from all sources for the year 1943.



The questions presented by the pleadings and the evidence in this proceeding are:

1. Whether petitioner is entitled to a foreign tax credit under the provisions of section 131 of the Internal Revenue Code on account of the tax on its net premiums received in the Dominion of Canada and imposed by and paid to that country for the taxable years 1942 and 1943 pursuant to the provisions of the Canadian Special War Revenue Act of 1915, as amended.

2. If it should be determined that such credit is allowable, then the further question is whether the limitation upon the amount of the foreign tax credit for insurance companies such as petitioner is to be measured on the basis of the ratio of the "normal tax net income" from Canadian sources to "Normal tax net income" from all sources or on the basis of the ratio of the taxable amount of income from Canadian sources to the taxable amount of income from all sources. We do not get to the second question unless the first is decided in petitioner's favor.

Petitioner concedes that prior to the amendment of section 131 by the Revenue Act of 1942 the decisions of the courts were against it. Some of these cases were: *The Continental Insurance Co.*, 40 B.T.A. 540; *St. Paul Fire & Marine Ins. Co. v. Reynolds*, 44 Fed. Supp. 863, 29 AFTR 592. But petitioner strongly contends that by the enactment of section 131(h) carried in the 1942 Revenue Act and applicable to all taxable years after December

31, 1941, Congress broadened the base for the allowance of these foreign income tax credits and included in such credit allowance taxes imposed on a corporation "in lieu" of an income tax. Petitioner contends that the taxes for which it here claims credit were levied by the Dominion of Canada "in lieu" of income taxes.

Respondent contends that the Canadian tax on petitioner's net premiums for which credit is claimed is not a tax paid "in lieu of a tax upon income" as that phrase is used in subsection (h) of section 131 which may be allowed as a credit under the provisions of section 131(a)(1), but is an excise tax or a business privilege tax. The pertinent provisions of section 131 of the Internal Revenue Code are printed in the margin.<sup>6</sup> Subsec-

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<sup>6</sup>Sec. 131. Taxes of Foreign Countries and Possessions of United States.

(a) Allowance of Credit.—If the taxpayer chooses to have the benefits of this section, the tax imposed by this chapter, except the tax imposed under section 102, shall be credited with:

(1) Citizens and domestic corporations.—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States; and

\* \* \*

(h) Credit for Taxes in Lieu of Income, Etc., Taxes.—For the purposes of this section and section 23(c)(1), the term "income, war-profits, and excess-profits taxes" shall include a tax paid in lieu of a tax upon income, war-profits, or excess-profits other-

tion (h) of section 131 was adopted as section 158(f) of the Revenue Act of 1942. At the time of the enactment of the above amendment to the Internal Revenue Code the Senate Finance Committee in its report (Report No. 1631, 77th Cong., 2nd Sess., p. 131) made the following pertinent comment:

Your committee believes further amendments should be made in section 131. Under that section as it now stands, a credit is allowed against United States Tax for income, war profits, or excess profits taxes paid or accrued to any foreign country or to any possession of the United States. In the interpretation of the term "income tax," the Commissioner, the Board, and the Courts have consistently adhered to a concept of income tax rather closely related to our own, and if such foreign tax was not imposed upon a basis corresponding approximately to net income it was not recognized as a basis for such credit. Thus, if a foreign country in imposing income taxation authorized, for reasons growing out of the administrative difficulties of determining net income or taxable basis within that country, a United States domestic corporation doing business in such country to pay a tax in lieu of such income tax but measured, for example, by gross income, gross sales or a number of units produced within

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wise generally imposed by any foreign country or by any possession of the United States.

[Subsection (h) was added to the Internal Revenue Code by section 158(f) of the Revenue Act of 1942.]

the country, such tax has not heretofore been recognized as a basis for credit. Your committee has deemed it desirable to extend the scope of this section. Accordingly, subsection (f) of section 160 provides that the term "income, war profits, and excess profits taxes" shall, for the purpose of sections 131 and 23(c)(1), include a tax paid by a domestic taxpayer in lieu of the tax upon income, war profits, and excess profits taxes which would otherwise be imposed upon such taxpayer by any foreign country or by any possession of the United States. \* \* \*

The premium tax here involved was first imposed by the provisions of the Special War Revenue Act of Canada which was enacted in 1915. The first income tax law of Canada known as the Income War Tax Act was enacted in 1917. Both acts have been in force since these dates and have been amended from time to time. The 1917 income tax act excepted from its provisions the income of mutual corporations such as petitioner not having a capital represented by shares, no part of the income of which inured to the profit of any member thereof. The rates of the net premium tax levied by the Special War Revenue Act of 1915 were increased by an amendment to that act in 1942 so that mutual fire insurance companies such as petitioner had their rates increased to three per cent. In 1946 the Special War Revenue Act of 1915, as amended, was again amended decreasing the rate of tax and the name of the act was changed to the "Canadian Excise Tax Act." In 1946 as a result



of an amendment to the Income War Tax Act of 1917, petitioner became subject to the income tax act but the tax on net premiums under the Special War Revenue Act was not removed. It was decreased from three per cent to two per cent.

The term "in lieu of" means in place of, instead of, or substituted for. See Webster's New International Dictionary (Second Edition, Unabridged.) *State v. Minneapolis & St. L. R. Co.*, 283 N. W. 244; *Mass. Bonding & Ins. Co. v. Rutley Const. Co.*, 287 N.Y.S. 662, 159 Misc. 392. That the Canadian premium tax does not qualify as a tax "in lieu of a tax upon income" seems to us to be quite apparent from the nature of the tax and from its history as set forth above. Prior to the enactment of subsection (h), *supra*, it had been held that the Canadian premium tax was not an income tax within the meaning of section 131(a)(1) of the Revenue Acts of 1932 and 1934 (similar to section 131(a)(1), I.R.C.) but was in the nature of an excise tax. *St. Paul Fire & Marine Ins. Co. v. Reynolds*, *supra*; *Continental Insurance Co.*, *supra*. Cf. *Helvering v. Queen Ins. Co.*, 115 Fed. (2d) 341. In the *Continental Insurance Co.* case we had before us the Special Canadian War Revenue Act of 1915 before it was amended by the War Revenue Act of 1942 and of it we said:

\* \* \* The law in question imposed a tax of one per cent upon the net premiums received by an insurance company in Canada, less net premiums paid for reinsurance to other companies subject to the act. Net premiums were defined as gross prem-



iums received, less rebates and returns. Thus the tax was imposed upon the gross premiums for risks taken by the company. The insurance did not have to result in a profit to subject the company to the tax. It was more like an excise tax upon the privilege of doing business than like an income tax. \* \* \*

In *St. Paul Fire & Marine Ins. Co. v. Reynolds*, supra, the court said: "Taxes imposed on insurance premiums for the privilege of transacting business long have been designated as an 'excise tax'." An excise tax is a charge for the privilege of following an occupation or trade, or carrying on a business. *Vinuo v. City of Seattle*, 120 Pac. 2nd 464, 11 Wash. 2nd 630; *Saviers v. Smith*, 128 N.E. 269, 101 Ohio St. 132. Cf. *Keasbey & Mattison Co. v. Rothensies*, 133 Fed. (2d) 894; *Commissioner of Insurance v. Commonwealth Mutual Liability Ins. Co.*, 32 N.E. 2nd 231, 308 Mass. 385.

We think it clear from the Senate Finance Committee's Report, heretofore quoted, that what Congress had in mind in providing in section 131(h) for a credit for a tax "in lieu of tax upon income," was a tax which was clearly a substitute for an income tax and not a tax imposed for the privilege of doing business in a foreign country. If the Canadian Government had first imposed the premium tax upon insurance companies in connection with the enactment of its Income War Tax Act in 1917 there might be some justification for saying that it was a substitute for a tax upon income and was to be measured by the amount of premiums collected but this premium tax was imposed in 1915, before

the income tax law was enacted. It was an excise tax at that time and its character as such was not changed by the subsequent enactment of the Income Tax Law of 1917. When the Canadian Government in 1946 decided to subject mutual insurance companies such as petitioner to income tax it did not eliminate the tax upon net premiums collected by such mutual insurance companies, it only decreased them. This, we think, as well as the whole history of the Canadian premium tax clearly indicates that Canada considered the premium tax as a separate and distinct tax from the income tax and not "in lieu" thereof. The fact that our Congress in the 1942 Revenue Act added section 131(h) so as to broaden the scope of the credit allowable under 131(a)(1) did not, in our opinion, change the character of the Canadian premium tax levied by its Special War Revenue Act of 1915, as amended, and make of it a tax levied in lieu of an income tax.

The instant case is distinguishable from *New York & Honduras Rosario Mining Co. v. Commissioner*, 168 Fed. (2d) 745, reversing 8 T.C. 1232 and *Santa Eulalia Mining Co.*, 2 T.C. 241. Both cases involved the allowance of a credit under section 131(a)(1) without reference to the later provisions contained in 131(h). In the *New York & Honduras Rosario Mining Co.* case the court said with reference to the tax there involved:

What a tax is called does not determine whether it is an income tax or an excise tax. *Flint v. Stone Tracy Co.*, 220 U. S. 107, 145. But we think it not

without significance that Honduras in its Mining Code does lay genuine excises, with forfeiture of the mining company's rights for non-payment, and also a tax on "liquid profits," without such forfeiture for non-payment, which is called an "income tax" in the contract approved by the national congress. Moreover, the tax on "liquid profits" is applicable to all miners, not merely to United States companies, and in general characteristics is indistinguishable from our own income tax. \* \* \*

In the Santa Eulalia Mining Co. case, *supra*, after analyzing the tax in question, we said:

Thus, we have a tax which is repeatedly referred to in the levying statute as an income tax and which is computed on the basis of petitioner's gross revenue from its mining properties. Although the method of determining the tax does not conform strictly to that by which income taxes are computed under our own laws, we do not think that that determines the nature of the tax.

Thus, in both of the above cases it was determined that the tax in question was in effect an income tax and, therefore, allowable as a credit under section 131(a)(1), I.R.C.

In the instant case, as we have endeavored to point out, the Canadian net premiums tax was neither an income tax nor was it a tax levied in lieu of an income tax. Therefore, the credit which petitioner claims cannot be allowed.

Having decided that petitioner is not entitled to the credit under section 131(a)(1) for the premium

taxes paid to Canada, it is unnecessary to discuss issue 2.

Reviewed by the Court.

Decision will be entered for the respondent.

Van Fossan, J., dissents.

[Seal]

Served Mar. 30, 1949.

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The Tax Court of the United States  
Washington

Docket No. 16147

NORTHWESTERN MUTUAL FIRE ASSOCIA-  
TION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### DECISION

Pursuant to the determination of the Court as set forth in its Opinion, promulgated March 30, 1949, it is

Ordered and Decided: That there are deficiencies in income taxes for the years 1942 and 1943 in the respective amounts of \$5,089.03 and \$5,347.81.

[Seal]     /s/ EUGENE BLACK,  
Judge.

Endorsed Mar. 30, 1949.

Served Mar. 31, 1949.

[Title of Tax Court and Cause.]

## PETITION FOR REVIEW

To the Honorable, the Judges of the United States  
Court of Appeals for the Ninth Circuit:

The petitioner, the Northwestern Mutual Fire Association, by Jo D. Cook, its counsel, hereby files its petition for a review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court of the United States rendered on March 30, 1949, determining that the petitioner was not entitled to a refund of \$10,183.13 for the year 1942 and was not entitled to a refund of \$10,854.73 for the year 1943 and determining a deficiency of \$5,089.03 for the year 1942 and a deficiency of \$5,-347.81 for the year 1943.

In support of this its petition for review filed in pursuance of the provisions of Sections 1141 and 1142 of the Internal Revenue Code, the petitioner respectfully shows:

### I.

#### Jurisdiction

The petitioner is a mutual fire insurance corporation organized and operating under the laws of the State of Washington. Its principal office is located at 217 Pine Street, Seattle, Washington. The petitioner filed its federal income tax returns for the years 1942 and 1943 with the Collector of Internal Revenue at Tacoma, Washington, whose office is located within the jurisdiction of the United States Court of Appeals for the Ninth Circuit.



## II.

## Prior Proceedings

This case was tried on the basis of stipulated facts before the Honorable Eugene Black, one of the Judges of the Tax Court of the United States on May 17, 1948, at Seattle, Washington. The Tax Court rendered its decision in favor of the respondent, and the decision was entered March 30, 1949.

## III.

## Nature of Controversy

This case involves an asserted deficiency in income tax for the years 1942 and 1943. The asserted deficiency is based upon a disputed claim for foreign tax credits under the provisions of Section 131(h) of the Internal Revenue Code.

For the year 1942 the petitioner claims a foreign tax credit in the total amount of \$15,272.16, whereas for said year the Commissioner of Internal Revenue asserts a deficiency in the amount of \$5,089.03.

For the year 1943 petitioner claims a foreign tax credit in the total amount of \$16,202.54, whereas the Commissioner of Internal Revenue for said year asserts a deficiency in the total amount of \$5,347.81.

## IV.

## Assignments of Error

That in its decision the Tax Court erred in the following particulars, to-wit:

A. In refusing to allow petitioner foreign tax

credits of \$15,272.16 for the year 1942 and \$16,202.54 for the year 1943;

B. In refusing to allow petitioner refunds of overpayments of income taxes in the amounts of \$10,183.13 for the year 1942, and \$10,854.72 for the year 1943;

C. In deciding that petitioner was liable for deficiencies in income taxes for the years 1942 and 1943 in the respective amounts of \$5,089.03 and \$5,347.81.

D. In deciding that petitioner was not entitled to the foreign tax credits claimed under Section 131 of the Internal Revenue Code.

E. In failing to decide that Section 131(b) of the Internal Revenue Code for the tax years referred to herein did not limit the amount of petitioner's foreign tax credit.

Wherefore, the petitioner petitions that the decision of the Tax Court of the United States be reviewed by the United States Court of Appeals for the Ninth Circuit, that a transcript of the record be prepared in accordance with the law and with the rules of said Court and transmitted to the Clerk of said Court for filing, and that appropriate action be taken to the end that the errors complained of may be reviewed and corrected by said Court.

/s/ JO D. COOK,

Counsel for Petitioner.

State of Washington,  
County of King—ss.

Jo D. Cook, being duly sworn, says that he is counsel for the Northwestern Mutual Fire Association, the petitioner herein, and as such is duly authorized to verify the petition for review by the United States Court of Appeals for the Ninth Circuit of the decision in the above entitled case; that he has read the said petition and is familiar with the statements therein contained; and that the statements made are true to the best of his knowledge, information and belief.

/s/ JO D. COOK,

Subscribed and sworn to before me this 21st day of June, 1949.

[Seal] /s/ GERTRUDE M. POHLE,

Notary Public for State of Washington Residing at  
Seattle, Washington.

My Commission expires November 4, 1952.

Filed June 24, 1949 T.C.U.S.

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[Title of Tax Court and Cause.]

## NOTICE OF FILING PETITION FOR REVIEW

To: The Commissioner of Internal Revenue, Respondent, and Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, Washington, D. C., Attorney for Respondent.

You are hereby notified that the petitioner did,

on June 24th, 1949, file with the Clerk of the Tax Court of the United States at Washington, D. C., a petition for review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court of the United States heretofore rendered in the above entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this 21st day of June, 1949.

/s/ JO D. COOK,

Counsel for Petitioner.

Personal service of the foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 24th day of June, 1949.

/s/ CHARLES OLIPHANT,

C.A.R.

Filed June 24, 1949 T.C.U.S.

[Title of Tax Court and Cause.]

### STIPULATION

It is Hereby Stipulated and Agreed by and between the parties to the above entitled action, through their respective counsel, that the record on appeal in this action shall include all of the pleadings, stipulations and documents of record in the above entitled Court.

/s/ JO D. COOK,

Counsel for Northwestern Mutual Fire Association,  
Appellant.

/s/ CHARLES OLIPHANT,

C.A.R.

Counsel for Commissioner of  
Internal Revenue, Appellee.

Filed Aug. 4, 1949 T.C.U.S.

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[Title of Tax Court and Cause.]

### CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States do hereby certify that the foregoing documents, 1 to 35 inclusive, constitute and are all of the original papers and proceedings on file in my office as the original and complete record in the proceeding before The Tax Court of the United States entitled "Northwestern Mutual Fire Association, Petitioner v. Commissioner of Internal



Revenue, Respondent, Docket No. 16147 and in which the petitioner in the Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 9th day of August, 1949.

[Seal]      /s/ VICTOR S. MERSCH,  
Clerk.

[Endorsed]: No. 12338. United States Circuit Court of Appeals For the Ninth Circuit. Northwestern Mutual Fire Association, a Corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review a Decision of The Tax Court of the United States.

Filed August 26, 1949.

      /s/ PAUL P. O'BRIEN,  
Clerk of the United States Circuit Court of Appeals  
for the Ninth Circuit.

United States Court of Appeals  
for the Ninth Circuit

No. 12338

NORTHWESTERN MUTUAL FIRE ASSOCIA-  
TION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

STATEMENT OF POINTS ON WHICH  
PETITIONER INTENDS TO REPLY

Comes now the Petitioner above named by and through its duly appointed counsel and advises the Court that the Petitioner intends to rely upon the Assignments of Error set forth in Paragraph IV of Petitioner's Petition for Review, which is made a part of the record herein.

/s/ JO D. COOK,

Counsel for Petitioner.

Filed Sept. 9, 1949 U.S.C.A.

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[Title of Court of Appeals and Cause.]

PETITIONER'S DESIGNATION OF RECORD  
TO BE PRINTED

Comes now the Petitioner above named by and through its duly designated counsel and designates

the following portion of the record in the above entitled case as the only portions of said record which are material to the consideration of the appeal:

I.

Referring to the transcript of the docket of the Tax Court, the Petitioner designates the following documents:

The Petition—Document No. 2.

Answer—Document No. 4.

Stipulation (less exhibits attached thereto)—Document No. 10 also No. 13.

Tax Court's Opinion—Document No. 30.

Tax Court's Decision—Document No. 31.

Petition for Review and Proof of Service—Document No. 32.

Stipulation re Contents of Record on Appeal—Document No. 35.

/s/ JO D. COOK,

Counsel for Petitioner.

Filed Sept. 9, 1949 U.S.C.A.



**In The United States Court of Appeals**  
**For the Ninth Circuit**

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NORTHWESTERN MUTUAL FIRE ASSOCIATION,  
*Appellant,*

vs.

COMMISSIONER OF INTERNAL REVENUE,  
*Appellee.*

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UPON APPEAL FROM THE TAX COURT OF THE  
UNITED STATES

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**APPELLANT'S OPENING BRIEF**

---

JO DUDLEY COOK,  
FREDERICK J. ORTH,

*Of Counsel:* *Attorneys for Appellant.*

RODE, COOK & WATKINS,  
217 Pine Street,  
Seattle 1, Washington.

DEC 19 1949





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**In The United States Court of Appeals**  
**For the Ninth Circuit**

<hr/>		
NORTHWESTERN MUTUAL FIRE ASSOCIA-	}	<b>No. 12338</b>
TION,		
vs.		
COMMISSIONER OF INTERNAL REVENUE,		
<i>Appellant,</i>		
<i>Appellee.</i>		
<hr/>		

UPON APPEAL FROM THE TAX COURT OF THE  
UNITED STATES

**APPELLANT'S OPENING BRIEF**

**Section C**

**JURISDICTION OF THE TAX COURT AND THIS COURT**

This action was commenced October 14, 1947, by appellant filing a petition in the Tax Court of the United States (Tr. 2, 4) wherein appellant, Northwestern Mutual Fire Association, a corporation under the laws of the State of Washington, was Petitioner and the Commissioner of Internal Revenue was respondent. The purpose of that action was to obtain a refund of \$21,037.86 of appellant's income tax paid for the years 1942 and 1943; and to set aside deficiency assessments by the Commissioner of Internal Revenue for said years in the amount of \$10,436.84 (Tr. 5).

The statutory provisions believed to sustain the jurisdiction of the Tax Court of the United States are Title V, ch. 619, §504(a), (c), 56 Stat. at L. 957, 26

U.S.C.A. 411, §1101; Title I, ch. 619, §168(a), 56 Stat. at L. 876, 26 U.S.C.A. 126, §272(a).

On March 30, 1949, the Tax Court rendered its decision and entered judgment denying appellant a refund and asserting deficiencies in its income tax in 1942 and 1943 in the respective amounts of \$5,089.03 and \$5,347.81 (Tr. 3, 66). An appeal therefrom was taken by appellant by Notice of Appeal filed on June 24, 1949 (Tr. 3, 67) .

The statutory provision believed to sustain the jurisdiction of this court is Title V, ch. 619, §504(a), (c), 56 Stat. at L. 957; 26 U.S.C.A. 514, §1141(a), (b).

It is well established that where the meaning of a statute of general application is involved and where there has been a failure of the Tax Court to apply correctly the law and regulations thereunder, questions are raised which are reviewable by this court.

*Dobson v. Commissioner* (1943) 320 U.S. 489, 492, 88 L. ed. 249, 64 S. Ct. 239, 31 A.F.T.R. 773;

*Bingham Trust v. Commissioner* (1944) 325 U.S. 365, 370, 371, 89 L. ed. 1670, 65 S. Ct. 1232, 33 A.F.T.R. 842;

*Commissioner v. Wilcox* (1945) 327 U.S. 404, 410, 90 L. ed. 752, 66 S. Ct. 35, 34 A.F.T.R. 811;

*Commissioner v. Swent* (4th C.C.A. 1946) 155 F.(2d) 513, 514, 34 A.F.T.R. 1376;

*Mutual Fertilizer Co. v. Commissioner* (5th C.C.A. 1947) 159 F.(2d) 470, 471, 35 A. F.T.R. 792;



*Kimbrell's Home Furnishings, Inc. v. Commissioner* (4th C.C.A. 1947) 159 F.(2d) 608, 610, 35 A.F.T.R. 824.

### Section D

#### STATEMENT OF THE CASE

This case involves a dispute between appellant and Appellee over the interpretation and application of sub-sections (h) and (b) Section 131 of the Internal Revenue Code as amended in 1942.

Appellant claims that under the provisions of these sub-sections it is entitled to a foreign tax credit for 1942 in the amount of \$15,272.16, whereas for that year the Commissioner of Internal Revenue [hereinafter referred to as the Commissioner] asserts a deficiency in the amount of \$5,089.03. For 1943 appellant claims a foreign tax credit in the amount of \$16,202.54, whereas for that year the Commissioner asserts a deficiency of \$5,347.81.

Appellee's reasons for disallowing the foreign tax credit claimed by appellant and asserting the deficiencies are stated in the deficiency notice as follows:

"The foreign tax credits claimed in your income tax returns for the calendar years 1942 and 1943 in the respective amounts of \$5,076.60 and \$5,339.84 as income taxes paid to the Dominion of Canada have been disallowed for the reason that the stated taxes do not constitute 'income, war profits, or excess profits taxes paid in lieu of a tax upon income, war profits or excess profits otherwise generally imposed' by Canada. The evidence indicates that the taxes in question were in the nature of an excise imposed

under the Special War Revenue Act of Canada, and therefore do not meet the requirements of Section 131 of the Internal Revenue Code in respect to allowable credits.

“For the stated reason it has been determined also that your claim for refund in the respective amounts of \$10,183.13 and \$10,854.73 should be disallowed for the years 1942 and 1943. The claims for refund are disallowed on the additional ground that a proper application of the provisions of Section 131 of the Internal Revenue Code negatives the use of investment income as the basis for computing the limitation factor provided for under sub-section (b) thereof, in the case of a mutual insurance company (other than life or marine) paying a tax based upon ‘the gross amount of income’ as defined in Section 207 of the Internal Revenue Code.” (Tr. 16, 17)

By appropriate assignments of error the appellant contested the Commissioner’s ruling and interpretation of sub-sections (b) and (h) of Section 131 I.R.C. for the reason that: The taxes paid by appellant to the Dominion of Canada under the provisions of the Special War Revenue Act of Canada as amended constituted “\* \* \* taxes paid in lieu of a tax on income, otherwise generally imposed” by Canada within the meaning of Section 131(h) I.R.C. (Tr. 5).

Appellant contends that it is entitled to the entire amount of the foreign tax credit claimed because a proper application of the provisions of Section 131(b) of the Internal Revenue Code requires the use of its normal-tax net income as the basis for computing the limitation factor provided for in that section.

The only dispute between appellant and appellee being over the interpretation of the law, they agreed to submit the case to the Tax Court upon a stipulation of facts with joint exhibits attached thereto (Tr. 24-42). The case was heard before the Tax Court on May 17, 1948, at which time oral arguments were waived and the stipulation of the parties was filed (Tr. 2, 43-47). Appellant and appellee having submitted briefs the Tax Court rendered its decision on March 30, 1949, Judge Van Fossen dissenting. The decision was entered on the same date (Tr. 3, 48-66). In its decision the Tax Court followed the Commissioner's interpretation of Section 131(h) I.R.C. in every respect, holding that the taxes paid by the appellant under the provisions of the Canadian Special War Revenue Act as amended were not taxes paid "in lieu of" a tax on income within the meaning of that section. Having decided against the appellant on that question the Tax Court did not express an opinion regarding the Commissioner's interpretation of subsection (b) of Section 131 I.R.C. (Tr. 65, 66).

Appellant served and filed timely notice of appeal from the decision of the Tax Court (Tr. 3, 67-71). The Tax Court adopted the stipulation of facts and joint exhibits (Tr. 24, 42) as their findings of fact (Tr. 50). The pertinent facts may be summarized as follows (Tr. 50-58):

Appellant is a mutual fire insurance corporation organized and operating under the laws of the State of Washington and is duly authorized and engaged in the business of writing insurance against the perils of fire and allied lines in all states of the United



States and in Canada, with its principal office in Seattle, Washington. Its income tax returns for the years 1942 and 1943 were prepared on the accrual basis and were filed with the Collector of Internal Revenue for the District of Washington at Tacoma, Washington, within and under extensions of time allowed by the Commissioner (Tr. 24, 50).

In 1942 and 1943 the appellant paid to the Dominion of Canada amounts in Canadian funds equivalent to \$15,272.16 and \$16,202.54 respectively in United States funds in taxes in accordance with the provisions of the Canadian Special War Revenue Act of 1915 as amended in 1942 (Tr. 29, 50). That tax was based upon the "net premiums" of appellant on its business in Canada and for those years the tax rate applicable to appellant was 3% (Tr. 29, 50).

In appellant's returns for the years 1942 and 1943 it claimed foreign tax credits in the respective amounts of \$5,076.60 and \$5,339.84 (Tr. 26, 51). It filed timely claims for refunds claiming additional foreign tax credits in the respective amounts of \$10,183.13 and \$10,854.73 for 1942 and 1943 (Tr. 26, 27).

Appellant's gross amount of income for the years 1942 and 1943 from all sources was \$6,716,320.72 and \$7,045,067.97 respectively, and its gross amount of income from sources in the Dominion of Canada (converted to U. S. funds) was \$507,681.54 and \$533,987.07 respectively (Tr. 28, 51).

In 1942 and 1943 appellant's normal-tax net income from all sources was \$126,451.85 and \$151,828.23 respectively, while for those years appellant's normal-

tax net income from sources in the Dominion of Canada (converted to U. S. funds) was \$37,843.46 and \$40,943.06 respectively (Tr. 27, 52).

During 1942 and 1943 appellant was not liable to tax on its net income from Canadian business under the provisions of the Canadian Income War Tax Act of 1917 as amended by Chapter 97, the provisions of which are set forth in the revised statutes of Canada of 1927 (Tr. 28, 52).

Prior to 1942 the appellant was required by the provisions of the Special War Revenue Act of 1915 to pay to the Dominion of Canada a tax of 1% on its net premiums from its business within the Dominion of Canada (Tr. 32, 53).

In 1942 the Dominion of Canada amended the Special War Revenue Act of 1915 by the enactment of Chapter 32 of the statutes of 1942 (Tr. 32, 53) increasing the tax on all fire insurance companies doing business in Canada, including the appellant, and the basis for said tax was the "net premiums" of said companies from their business within the Dominion of Canada. For all mutual fire insurance companies, such as the appellant, not subject to taxation on their net income under the provisions of the Canadian Income War Tax Act of 1917, the rate was increased from 1% to 3%. For all fire insurance companies which were subject by Canadian law to taxation on their net income under the Income War Tax Act of 1917 (which did not include this appellant) the rate was increased from 1% to 2% (Tr. 33, 53).

In 1946 the Canadian revenue measures were revised and the Income War Tax Act originally enacted



in 1917 was amended so that mutual fire insurance companies, such as appellant (excepting only those mutual fire insurance companies deriving their premiums wholly from the insurance of churches, schools or other religious, educational or charitable institutions), were made subject to the general income tax law of Canada (Tr. 36, 54). Prior to the enactment in 1946 of the above amendment to the Income War Tax Act of 1917 mutual fire insurance companies such as appellant were not liable to tax under the provisions of the Income War Tax Act of 1917 (Tr. 28, 55) (Appendix No. XIX).

Concurrent with the change in 1946 in the Income War Tax Act of 1917 the Special War Revenue Act of 1915 was amended further changing the name of the act from "Special War Revenue Act" to the "Canadian Excise Tax Act," and said amendment further provided that the rate of tax upon the net premium for mutual fire insurance companies such as appellant should be reduced from 3% to 2% (Tr. 38, 55).

In 1942 and 1943 the taxes imposed under the Special War Revenue Act of 1915 as amended, and the Income War Tax Act of 1917 as amended, were paid to the Minister of National Revenue, sometimes referred to as the Minister of Finance (Tr. 35, 56).

In 1942 and 1943 the administrative details of collection and auditing of taxes payable by insurance companies under the Special War Revenue Act of 1915 as amended, and the auditing of income tax returns of insurance companies which were subject to the provisions of the Income War Tax Act as amended were handled by the Department of Insurance (Tr. 35, 56).

In 1942 and 1943 the details of collection and auditing of taxes other than taxes on insurance companies payable under the Special War Revenue Act of 1915 as amended, and the general administration and the auditing of returns of taxpayers other than insurance companies under the Income War Tax Act of 1917, were handled by the Department of National Revenue (Tr. 35, 56).

In its returns for the years 1942 and 1943 and in the statement in support of credit for the foreign tax paid (Form 1118) for those years, appellant computed its foreign tax credit on the basis of its gross amount of income for each year (which constituted its taxable income under the statute). On that basis using the ratio of the total gross income from Canada (\$507,-681.54) for 1942, and \$533,987.07 for 1943) to total gross income in its returns from all sources for those years (\$6,715,077.99 for 1942 and \$7,044,271.09 for 1943) the amounts of the credits so computed were \$5,076.60 and \$5,339.84 for the years 1942 and 1943, respectively. The appellee disallowed the credits claimed by appellant in appellee's deficiency notice (Tr. 16, 17, 57).

In its claims for refunds for 1942 and 1943 and the statements in support of credit for foreign taxes attached thereto, appellant claimed that the credit for each year should be computed upon the basis which the ratio of the "normal-tax net income" from sources in Canada bears to the "normal-tax net income" from all sources. On that basis using the ratio which its normal-tax net income of \$37,843.46 from Canadian sources bears to the "normal-tax net income" of \$126,-

451.85 from all sources for 1942, and the ratio which its "normal-tax net income" of \$40,943.06 from Canadian sources bears to "normal-tax net income" of \$151,828.23 from all sources for 1943, the allowable foreign tax credit amounts to \$15,272.16 and \$16,202.54 for 1942 and 1943, respectively (Tr. 12, 41, 57).

The appellee denied appellant's claim for foreign tax credit and appellant's claim for refund of taxes paid on two grounds. First, on the ground that the taxes paid by it to the Dominion of Canada under the provisions of the Special War Revenue Act of Canada were not taxes paid "in lieu of a tax on income" within the meaning of Section 131(h) I.R.C. Secondly, on the ground that the provisions of Section 131(b) I.R.C. negatives the use of "normal-tax net income" as the basis for computing the limitation factor provided for in said section in the case of a mutual insurance company (other than life or marine) such as appellant, paying a tax based upon "the gross amount of income" as defined in Section 207 I.R.C. (Tr. 16, 17, 49).

The Tax Court held that the tax paid by the appellant to the Dominion of Canada under the provisions of the Special War Revenue Act were not taxes paid "in lieu of a tax on income" within the meaning of Section 131(h) I.R.C., and did not express an opinion regarding the interpretation of the limitation feature of Section 131(b) I.R.C. (Tr. 65, 66).

On this appeal, therefore, the following questions are presented. (1) whether appellant is entitled to a

foreign tax credit under the provisions of Section 131(h) I.R.C. on account of taxes paid by it to the Dominion of Canada for the years 1942 and 1943 under the provisions of the Canadian Special War Revenue Act of 1915 as amended? The Tax Court answered this question in the negative (Tr. 58, 65), (2) whether the limitation upon the amount of appellant's foreign tax credit under the provisions of Section 113(b) IR..C., is measured by the ratio of appellant's "normal-tax net income" from Canadian sources to "normal-tax net income" from all sources? Having answered the first question in the negative the Tax Court declined to answer this question. Appellant contends that both of the above questions should be answered in the affirmative (Tr. 58, 65).

## Section E

### SPECIFICATION OF ERRORS

It is respectfully submitted that the Tax Court erred in the following particulars:

#### I.

In deciding that appellant was not entitled to the foreign tax credit claimed under the provisions of Section 131(h) I.R.C.

a. In failing to allow appellant foreign tax credits of \$15,272.16 for 1942, and \$16,202.54 for 1943.

b. In failing to allow appellant refunds of over payments of income taxes in the amounts of \$10,183.13 for 1942, and \$10,854.72 for 1943.

c. In deciding that appellant was liable for deficien-



cies in its income taxes for the years 1942 and 1943 in the respective amounts of \$5,089.03 and \$5,347.81.

## II.

In failing to decide that Section 131(b) I.R.C. required the limitation of appellant's foreign tax credit to be calculated on the basis of the ratio of its "normal-tax net income" from Canadian sources to its "normal-tax net income" from all sources, and that said subsection did not limit the amount of tax credit claimed by appellant.

### Section F

### ARGUMENT

#### Summary of Argument

The Tax Court denied appellant's foreign tax credit claim holding that the tax paid by it to the Dominion of Canada in 1942 and 1943 under the Canadian Special War Revenue Act was not a "tax in lieu of \* \* \* an income tax otherwise generally imposed" within the meaning of Section 131(h) I.R.C. It did not discuss the application of Section 131(b) I.R.C.

Appellant's principal argument under Section F of its brief is that the tax paid by it to Canada in 1942 and 1943 was a tax paid "in lieu of a tax on income otherwise generally imposed by a foreign country" within the meaning of Section 131(h). In support of its contention the literal meaning of Section 131(h) I.R.C. is discussed in Part I. The Commissioner's Regulation applicable to that section is discussed in Part II. Parts III and IV deal with the intent of Congress and the Canadian Parliament in that order, and each shows that it supports appellant's contention. In Part



V all pertinent rulings by the Commissioner are considered, and in Part VI the applicable cases, including the Tax Court's decision in this case, are analyzed showing how they support appellant's contention.

Appellant's argument under Section G of its brief deals with the interpretation and application of Section 131(b) I.R.C. The literal meaning of Section 131(b) I.R.C. is considered in Part I of that section. The applicable regulation of the Commissioner is discussed in Part II. Part III contains an explanation of that section and that regulation as applied to appellant. Part IV demonstrates that a literal interpretation of its terms is the only permissible construction of Section 131(b).

## I.

### **According to the Literal Meaning of Section 131 (h) I.R.C. Appellant Is Entitled to the Foreign Tax Credit Claimed.**

Section 131 of the Internal Revenue Code provides as follows:

*Sec. 131. Taxes of Foreign Countries and Possessions of the United State.*

“(a) Allowance of Credit:—If the taxpayer chooses to have the benefit of this section, the tax imposed by this chapter, except the tax imposed under section 102, shall be credited with:

“(1) Citizens and domestic corporations — In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, or excess-profits tax, paid or accrued during the taxable year to any foreign country or to any possession of the United States:

\* \* \* \* \*

“(h) Credit for Taxes in Lieu of Income, etc., Taxes—*For the purposes of this section and section 23(c) (1), the term ‘income, war-profits, and excess-profits taxes,’ shall include a tax paid in lieu of a tax on income, war-profits, or excess-profits otherwise generally imposed by any foreign country or by any possession of the United States.*” (Italics our) (See Appendix No. I)

The above quoted portions of Section 131 I.R.C. were applicable as quoted to the tax years 1942 and 1943 and were the sections under which the appellant claimed foreign tax credits.

Sub-section (h) above quoted was added to Section 131 of the Internal Revenue Code by Section 158(f) of the Revenue Act of 1942. Section 101 of the 1942 act makes this amendment applicable to the taxable years beginning after December 31, 1941.

For the tax years 1942 and 1943, appellant paid to the Dominion of Canada amounts in Canadian funds equivalent to \$15,272.16 and \$16,202.54, respectively in United States funds as taxes under the provisions of the Canadian Special War Revenue Act of 1915 as amended in 1942 (Tr. 29, 50). For those years appellant was exempt by law from paying, and did not pay to the Dominion of Canada any income tax under the provisions of Canada's Income War Tax Act, which was an income tax act generally imposed by Canada on other non-exempt corporations and individuals (Tr. 33, 52, 53).

It is conceded that Canada is a “foreign country” within the meaning of that term as used in Section 131(h) I.R.C.

Appellant contends that the taxes above referred to which were paid by it to the Dominion of Canada were taxes paid "in lieu of a tax on income otherwise generally imposed by any foreign country" within the meaning of Section 131(h) I.R.C. The appellee contends that the taxes referred to above were not taxes paid "in lieu of" a tax on income otherwise generally imposed.

Manifestly, since there is no dispute on the facts, it is necessary to interpret and construe the "in lieu of" provision of Section 131(h). In doing so it is necessary to employ the recognized rules of construction applied by the courts in interpreting and construing tax statutes of the United States. The following rules of construction are pertinent:

1. The intention or purpose of Congress in enacting or amending the particular law under consideration should be ascertained and the statute or amendment under consideration should be construed in such a way as to achieve and not defeat the aim or object of the enactment or amendment.

*Blake v. National City Bank of New York*  
(1875) 90 U.S. 119, 23 L. ed. 307, 2 A.F.  
T.R. 2339;

*Burnet v. Chicago Portrait Co.* (1932) 285  
U.S. 1, 76 L. ed. 587, 10 A.F.T.R. 800.

2. Tax statutes should be construed so as not to extend their provisions by implication beyond the clear import of the language used, but in cases of doubt the statutes are construed most broadly against the government and in favor of the citizen.

*Gould v. Gould* (1917) 245 U.S. 151, 152,  
62 L. ed. 211, 213, 3 A.F.T.R. 2958.

3. Where a statute was passed for a remedial purpose it should be liberally construed in the taxpayer's favor.

*United States v. Merriam* (1923) 263 U.S.  
179, 187, 68 L. ed. 240, 244, 29 A.L.R.  
1547, 44 S. Ct. 69, 4 A.F.T.R. 3673;

*Bonwit Teller & Co. v. United States* (1930)  
283 U.S. 258, 263, 75 L. ed. 1018, 1021,  
9 A.F.T.R. 1421;

*Kimbrell's Home Furnishings, Inc. v. Commissioner* (1947, 4th C.C.A.) 159 F.(2d)  
608, 610, 35 A.F.T.R. 824.

4. Where the meaning of particular words used in a tax statute are in doubt, the words should be construed according to their literal and popular meaning.

*Maillard v. Lawrence* (1853) 16 How. (U.S.)  
251, 261, 14 L. ed. 925, 930;

*United States v. Merriam* (1923) 263 U.S.  
179, 187, 68 L. ed. 240, 244, 29 A.L.R.  
1547, 44 S. Ct. 69, 4 A.F.T.R. 3673;

*Crooks v. Harrelson* (1930) 282 U.S. 55, 75  
L. ed. 156, 9 A.F.T.R. 571;

*Deputy v. DuPont* (1940) 308 U.S. 488, 84  
L. ed. 417, 23 A.F.T.R. 808.

With these rules of construction in mind it is pertinent to inquire what is the literal, ordinary, popular meaning of the phrase "in lieu of." "In lieu of" as used in this section must mean "in place of" or "instead of" because that is the literal meaning of the



phrase as defined in the Century Dictionary, Funk & Wagnells New Standard Dictionary and Webster's New International Dictionary (second edition) unabridged and as it is employed in the case of

*State v. Minneapolis St. L. R. Co.* (1939)  
283 N.W. 244.

According to the literal meaning of the language employed in Section 131(h), for the appellant to be entitled to a foreign tax credit, it must appear that the tax paid by it to Canada was a *tax paid "in place of" or "instead of" a tax on income otherwise generally imposed* by Canada. It *does not* require (as the Commissioner's deficiency notice states) that the tax must constitute "income \* \* \* taxes paid in lieu of a tax upon income \* \* \* otherwise generally imposed by Canada." Was the tax paid by appellant "*a tax paid in place of a tax on income otherwise generally imposed*" by Canada? During 1942 and 1943 Canada had a tax on income which was generally imposed upon corporations (Tr. 35, 36, 37, 54). Appellant was specifically exempt from the tax on income generally imposed upon other corporations (Tr. 28, 29, 52, 53). "Instead of" paying a tax to Canada under the provisions of the general income tax statute appellant paid a tax at the rate of 3% upon its net premium income under the provisions of the Special War Revenue Act (Tr. 29, 50). According to the non-technical, literal and popular meaning of the language employed in Section 131(h), the tax paid by appellant to the Dominion of Canada was a tax paid "in lieu of," "in place of," or "instead of" a tax on income otherwise generally imposed by Canada.



## II.

**According to the Commissioner's Regulations Interpreting Section 131 (h) I.R.C., Appellant Is Entitled to the Foreign Tax Credit Claimed.**

After the passage of the Revenue Act of 1942 the Commissioner promulgated Regulation 103, Section 19.131.2 (Appendix No. X). In the Commissioner's own interpretation of Section 131(h) he states:

"For the purpose of Section 131 \* \* \* the term 'income \* \* \* taxes includes \* \* \* a tax imposed by statute \* \* \* by a foreign country \* \* \* if (a) such country \* \* \* has in force a general income tax law; (b) the taxpayer claiming the credit would in the absence of a specific provision applicable to such taxpayer be subject to such general income tax, and (c) such general income tax is not imposed upon the taxpayer, thus subject to such substituted tax'." (Appendix No. X)

Significantly, the Commissioner indicates in his regulation that an "in lieu of" tax could be expected to be imposed where the ascertainment of "net income," though not the determination of "gross income" from sources in the foreign country was found administratively difficult.

That it is equally as difficult in Canada as in the United States to ascertain the "net income" of a mutual insurance company is obvious. The report of the U. S. Senate Committee on Finance in discussing its attempt to formulate an income tax law applicable to mutual insurance companies such as the appellant to be incorporated in the Revenue Bill of 1942 stated, in part, as follows:

"Your committee carefully considered the House Bill plan and various modifications of it in an attempt to define and tax underwriting income in an equitable manner. No adequate method to accomplish this result was developed.

\* \* \*" (See Appendix No. XIV)

The ascertainment of "net income" of mutual insurance companies was so difficult in our own country that provision was made in Section 207 I.R.C. to tax them on substantially a "gross income" basis. (Appendix Nos. II and XIV)

Under these circumstances it is not surprising that at the same time in Canada, appellant was subject, under the Special War Revenue Act, to a tax of 3% on its net premiums, which is, in effect, a tax on the basis of "gross income." Because of the administrative difficulty of ascertaining "net income" of mutual insurance companies such as appellant there was, in Canada, as in the United States, the same reason for a tax on mutual insurance companies such as appellant "in place of" a tax on their "net income."

Appellant does not question the validity of Commissioner's regulation. It is a correct interpretation of Section 131(h) I.R.C.. Appellant asks only that the terms of that regulation be properly applied to the facts of this case. What are the facts? Compare the requirements of the Commissioner's regulation and the pertinent facts of this case. The Commissioner's regulation requires:

(a) That such foreign country has in force a general income tax law:

During 1942 and 1943 Canada had in force a general income tax law (Tr. 35, 36, 54).

(b) That the taxpayer claiming the credit would in the absence of a specific provision applicable to such taxpayer be subject to such general income tax:

Appellant, the taxpayer in this case, in the absence of a specific provision applicable to it would have been subject to the general income tax law of Canada during 1942 and 1943 (Tr. 28, 29, 35, 36).

(c) That such general income tax was not imposed upon the taxpayer thus subject to such substituted tax:

Such general income tax law was not imposed upon the appellant taxpayer, thus subject to such substituted tax (Tr. 28, 29, 52, 53).

Appellant was subject to and did in fact pay a substituted tax of 3% on its net premiums in Canada, which amounted to \$15,272.16 in U. S. funds for 1942 and \$16,202.54 in U. S. funds for 1943 (Tr. 29, 50).

Having complied with the conditions precedent specified by the Commissioner in his regulation interpreting the provisions of Section 131(h) I.R.C., appellant is entitled to foreign tax credits in the above amounts as claimed.

## III.

**Construing the Provisions of Section 131 (h) I.R.C.,  
According to the Intent of Congress, Appellant Is  
Entitled to the Foreign Tax Credit Claimed.**

(a)

*The early historical background of the foreign tax credit section of the U. S. Internal Revenue Code indicates Congress intended to permit a foreign tax credit under the circumstances of this case.*

Appellee concedes that Section 131(h) must be construed to accomplish the result intended by Congress in adding sub-section (h) to Section 131 I.R.C. Appellant believes that to ascertain the true intent of Congress requires a thorough understanding of the historical background of the foreign tax credit section of the U. S. Internal Revenue Code.

Prior to the enactment of the Sixteenth Amendment to the Constitution of the United States the Supreme Court of the United States held the income tax law of 1895 (28 Stat. at L. 509) unconstitutional.

*Pollock v. Palmer's Loan & Trust Co.* (1895)  
157 U.S. 429, 39 L. ed. 759, 15 S. Ct. 673,  
3 A.F.T.R. 2557.

A lucrative source of revenue was thus denied to the government because of the direct tax and apportionment features of Article I, Section 2, Clause 3, and Article I, Section 9, Clause 4 of the Constitution. Faced with this problem Congress enacted the Tax Act of August, 1909 (36 Stat. at L. 11, §112-117, Chapter 6, U. S. Comp. Stat. Supp. 1909, Pages 659, 844, 849) providing that insurance companies and all cor-



porations, joint stock companies or associations organized for profit and having a capital stock represented by shares should be subject annually to a special excise tax for the privilege of doing business at the rate of 1% of their net income in excess of \$5,000.00, subject, however, to certain credits and deductions. A deduction from gross income was allowed to the corporation for all sums paid by it within the year for taxes imposed by the government of any foreign country as a condition to carrying on business therein (36 Stat. at L. 113, Chapter 6). In the case of *Flint v. Stone Tracy Company* (1911) 220 U.S. 107, 55 L. ed. 389, 31 S. Ct. 342, 3 A.F.T.R. 2834, the Supreme Court of the United States held that this tax was an excise tax and therefore constitutional. This was prior to the adoption of the Sixteenth Amendment to the United States Constitution, which was not ratified until 1913.

The significance of this historical data is two-fold. The deduction feature of the law was an early recognition by Congress that relief under U. S. tax statutes should be granted to corporations for taxes they were required to pay in foreign countries. The second pertinent observation respecting this historical data is that here in our own tax law is a classic example of a tax "in lieu of" an income tax within the literal meaning of that phrase. In 1895 Congress had attempted to enact an income tax law, but that law was declared unconstitutional. Having been thwarted in its attempt to pass a valid income tax law Congress passed the special excise tax law of 1909 above re-



ferred to "in place of," "instead of," or "in lieu of" an income tax law.

Upon the ratification of the Sixteenth Amendment to the Constitution the income tax act of October 3, 1913, was enacted. In Section G(b) of that act (38 Stat. at L. 173, Chapter 16) a deduction was allowed in computing the net income of a corporation for all sums paid by it within the year for taxes imposed under the authority of the United States or any state or territory thereof, or by the government of any foreign country. Similar provisions were contained in the income tax acts of September 8, 1916, §5(a), §6(a), and §12(a) (39 Stat. at L. 759, 769, Chapter 463), and in the income tax act amendment of October 3, 1917, §1201(1), §1207(1) (40 Stat. at L. 330, 335, Chapter 63). The special excise tax of August 5, 1909, was not reenacted or carried forward into the income tax act of October 3, 1913. It was repealed by paragraph S, Section IV, Chap. 16 of the act of October 3, 1913 (38 Stat. at L. 201).

In our earliest income tax laws Congress intended to give relief to domestic taxpayers operating in foreign countries by permitting them a deduction under the U. S. income tax law for taxes paid to a foreign government. The fact that the special 1% excise tax imposed under the provisions of the law of 1909 was not carried forward or re-enacted at the time the income tax act of 1913 was passed, indicates conclusively that it is a classic example in our own law of a tax "in lieu of" an income tax.

In the revenue act of 1918 there was a provision for a *credit* against income taxes levied in the United

States for taxes paid to any foreign country upon income derived from sources therein (Sections 222(a), 238(a), 40 Stat. at L. 1073, 1080, Chapter 18). With respect to Congress' change in policy in allowing a credit instead of a deduction the Supreme Court of the United States said:

"The distinction made with respect to \* \* \* deduction from gross income and credits against taxes simply reflects the economic policy adopted in making allowances for taxes paid within the borders of the continental United States and the organized territories. In relation to income taxes paid outside these borders, the provision as to credit was enacted to give greater, and not less, relief."

*Burnet v. Chicago Portrait Co.* (1932) 285  
U.S. 1, 15, 76 L. ed. 587, 594, 10 A.F.T.R.  
800.

With respect to the allowance of such credits as distinguished from deductions from gross income in computing net income, the Committee on Ways and Means of the House of Representatives in its report on the revenue bill of 1918 (H.R. Rep. No. 767, 65 Cong. Second Session, page 11) said:

"Under existing law a citizen of the United States can only deduct income, war or excess-profits taxes paid to a foreign country from gross income in computing net income. With the corresponding high rates imposed by certain foreign countries the taxes levied in such countries in addition to the taxes levied in the United States upon citizens of the United States, placed a very severe burden upon such citizens. The bill provides that a credit against the income tax im-

posed in the United States be allowed a citizen of the United States, subject to income and war or excess-profits taxes in a foreign country of an amount equal to the tax paid in such country upon income that is received from sources within such country. \* \* \*"

Furthermore, in the report of the Committee on Ways and Means of the House of Representatives in relation to the revenue bill of 1921 (H.R. Rep. No. 350, 67th Cong. First Session, page 8) the following statement was made with respect to American concerns doing business in foreign countries:

"Under existing law an American citizen or domestic corporation is taxed upon his or its entire income even though all of it is derived from business transacted without the United States. This results in double taxation, places American business concerns at a serious disadvantage in the competitive struggle for foreign trade, and even encourages American corporations doing business in foreign countries to surrender their charters and incorporate under the laws of foreign countries."

While this statement was made to introduce a remedial proposal which was not adopted it discloses the purpose of Congress in liberalizing the foreign tax provisions of U. S. Revenue measures up to that time, and further indicates a trend to broaden and liberalize the basis for allowing foreign tax credit relief to domestic corporations.

A similar foreign tax credit provision was carried over into the revenue act of 1921. Section 222 (a) (42 Stat. at L., 227, 258, 259 Chapter 136). The foreign tax credit provision of the revenue act of 1921

with certain minor changes has been incorporated in each revenue act thereafter up to and including the Internal Revenue Code as amended in 1942.

The obvious and consistent purpose of Congress in incorporating a foreign tax credit provision in our tax law has been to mitigate the evil of double taxation. The same controlling purpose is manifest in the foreign tax credit provision of the 1918 revenue act down to the present. The changes made by Congress in the foreign tax credit provisions of the various acts reveals an unmistakable trend towards a liberalization of the foreign tax credit provisions of our tax acts. By amending and liberalizing the foreign tax credit provisions Congress has sought to make those provisions carry out their purpose more effectively. Obviously the intent of Congress in adding subsection (h) to Section 131 I.R.C. was to broaden the basis for allowing foreign tax credits. Congress intended to have that particular section of the code carry out its purpose (of avoiding double taxation) more effectively, so that under the circumstances of this case appellant's Canadian income would not be subject to double taxation because a foreign tax credit could be allowed under that section as amended.



## (b)

*The historical background of Section 131 I.R.C. indicates Congress intended to permit a foreign tax credit under the circumstances of this case.*

Prior to the amendment of Section 131 I.R.C. in 1942 the Commissioner and the courts on many occasions had construed its terms (See Appendices XX, XXI, XXIII and XIV). These rulings and decisions will be discussed in subsequent parts, so at present a general observation respecting them will suffice. The Commissioner's rulings and the courts' decisions referred to apply the following test:

Was the foreign tax which was claimed as a foreign tax credit a "net income tax upon profits" within the meaning of those terms as employed in the U. S. tax law?

Only if, upon the basis of a very strict examination of the facts, this question could be answered in the affirmative was the foreign tax credit allowed.

An interesting case in point which is relied upon by the Commissioner is the decision of the United States District Court in the case of *St. Paul Fire & Marine Insurance Co. v. Reynolds* (March 9, 1942) 44 F. Supp. 863, 29 A.F.T.R. 592, which will be analyzed more completely in a succeeding part. In that case, applying the traditional test, the court held that the Canadian Special War Revenue tax was an excise tax, and for that reason the taxpayer could not be allowed a foreign tax credit under Section 131 (a) (1) I.R.C. prior to the addition of subsection (h) to Section 131 I.R.C. in 1942.



Considering that decision in its proper historical setting it supports appellant's contention that Congress intended a foreign tax credit to be allowed under the circumstances of this case.

The decision of the District Court in that case was rendered on March 9, 1942. Slightly less than seven months thereafter the Senate Finance Committee, having been deliberating on the amendment of Section 131 I.R.C., issued its report dated October 2, 1942, in which it submitted an amendment to Section 131 I.R.C. That proposed amendment became subsection (h) of Section 131 of the 1942 Internal Revenue Code. Referring to the reason for the addition of subsection (h) to Section 131 I.R.C., the Committee on Finance of the U. S. Senate stated:

“\* \* \* in the interpretation of the term ‘income tax’ the Commissioner, the Board and the court have consistently adhered to a concept of income tax rather closely related to our own, and if such foreign tax was not imposed upon a basis corresponding approximately to net income it was not recognized as a basis for such credit. Thus, if a foreign country imposing income taxation authorized for reasons growing out of administrative difficulties of determining net income or taxable basis within that country, a United States domestic corporation doing business in such country to pay a tax in lieu of such income tax, but measured by gross income, gross sales for a number of units produced within the country, such tax has not heretofore been recognized as a basis of credit.

“Your Committee has deemed it desirable to extend the scope of this section. Accordingly,

subsection (f) of Section 160 provides that the term 'income, war tax and excess profits tax' shall for the purposes of Sections 121 and 23c-1 include a tax paid by a domestic taxpayer in lieu of a tax upon income, war profits and excess profits taxes which would otherwise be imposed upon such taxpayer by any foreign country or by any possession of the United States." (Tr. 39, 60, 61)

It was the expressed intent of Congress to change the law upon which the United States District Court based its decision in the case of *St. Paul Fire & Marine Insurance Co. v. Reynolds*, *supra*. Clearly, Congress felt that the test employed by the court in that case and the test employed by the Commissioner and the courts in prior cases construing Section 131 was too circumscribed. The expressed intent of Congress in adding subsection (h) to Section 131 was "to extend the scope of this section."

It must be presumed that Congress, in amending Section 131 I.R.C., acted with full knowledge, not only of the terms of the existing statute on the subject, but also with full knowledge of the decisional law interpreting that section, including particularly the most recent construction of the statute by a Federal court prior to the amendment of that section; namely, the case of *St. Paul Fire & Marine Insurance Co. v. Reynolds*, *supra*.

*Johnson v. U. S.* (1911) 225 U.S. 405, 416,  
32 S. Ct. 748, 56 L. ed. 1142;

*Shamrock Oil & Gas Corporation v. Sheets*  
(1940) 313 U.S. 100, 106, 85 L. ed. 1215,  
1218, 61 S. Ct. 739;

*Barnidge v. U. S.* (8th C.C.A., 1939) 101 F.(2d) 295, 297;

*U. S. v. Stroop* (6th C.C.A., 1940) 109 F. (2d) 891, 893, 24 A.F.T.R. 422.

It is well established that change in a later income tax law from the phraseology of an earlier statute which has been given a settled construction by the Treasury Department is indicative of a legislative intention to make a change in the law.

*Brewster v. Gage* (1929) 280 U.S. 327, 337, 74 L. ed. 457, 463, 50 S. Ct. 115, 8 A.F. T.R. 10263.

It is likewise well settled that where a provision in a statute such as the one involved in this case is intended to be remedial, it must be construed liberally in the taxpayer's favor and must be allowed to prevail in case of conflict with pre-existing rules.

*Western Union Telegraph Co. v. Eyser* (1873) 19 Wall. (U.S.) 419, 22 L. ed. 43, 44;

*Bonwit Teller & Co. v. U.S.* (1930) 283 U.S. 258, 263, 75 L. ed. 1018, 1021, 51 S. Ct. 395, 9 A.F.T.R. 1421;

*Helvering v. Bliss* (1934) 293 U.S. 144, 151, 79 L. ed. 246, 251, 55 S. Ct. 17, 95 A.L.R. 207, 14 A.F.T.R. 668.

Congress must be presumed to have had the District Court's decision in the case of *St. Paul Fire & Marine Insurance Co. v. Reynolds* in mind when, as a remedial measure, it enacted the amendment adding subsection (h) to Section 131. It must be presumed

that Congress had in mind the Canadian Special War Revenue tax which was considered in that case as not eligible to foreign tax credit, when in the report by its Senate Committee on Finance it indicated that a foreign tax credit should be allowed for "a tax in lieu of such income tax but measured by gross income, gross sales, or a number of units produced within the country \* \* \*." The tax for which appellant claims a foreign tax credit is such a tax. That Congress intended to permit a foreign tax credit under the circumstances of this case seems clear. Any doubts regarding the interpretation or application of subsection (h) to this case must be resolved in appellant's favor.

(c)

***The historical background of the Internal Revenue Code as applied to mutual insurance companies such as appellant indicates Congress intended to permit a foreign tax credit under the circumstances of this case.***

It is evident from an examination of the historical development of the U. S. taxation policies that mutual insurance companies have been traditionally exempt from income taxes under Section 101(11), or a corresponding section of the Internal Revenue Codes prior to the 1942 amendment.

There are numerous sound and logical reasons for such exemption. Mutual insurance companies are non-profit organizations of the same general type that are customarily exempt from income taxation. In their operation, their system of transacting business is such that they do not develop a "net income" or "a profit" similar to that of business organizations that are sub-



ject to income taxation. Because such companies are fundamentally cooperative enterprises the purpose of which is to furnish insurance protection to members at cost, their purpose places them in a category different from that of the ordinary business enterprise which is subject to tax upon its net income.

The formulation of a satisfactory and equitable basis for taxing of mutual insurance companies has in the past proven administratively difficult. Such difficulty as previously indicated was appreciated by the Senate Committee on Finance, which was largely responsible for the preparation of the 1942 amendment which made appellant subject to taxation in the U. S. under Section 207 I.R.C., and which also added subsection (h) to Section 131 I.R.C. When the 1942 amendment to the Internal Revenue Code was under consideration the Senate Finance Committee in its report had this to say regarding the taxation of mutual insurance companies:

“Under the House Bill mutual insurance companies, other than life, were to be taxed on the basis of their underwriting and investment income. The objective was a taxing system substantially the same as that which has been applied to stock insurance companies other than life since 1921. \* \* \*

“Your committee carefully considered the House Bill plan and various modifications of it in an attempt to define and tax underwriting income (*of mutual insurance companies*) in an equitable manner. No adequate method to accomplish that result was developed. \* \* \*” (Italicized portion inserted) (Appendix No. XV)



Congress had its own experience in mind when in adding subsection (h) to Section 131 it indicated its intent to allow a foreign tax credit “\* \* \* if a foreign country imposing income taxation authorized by reasons growing out of administrative difficulties of determining net income or taxable basis within that country, a United States domestic corporation doing business in such country to pay a tax in lieu of such income tax but measured by gross income \* \* \*” (Tr. 39, 60).

Although mutual insurance companies such as the appellant have been traditionally exempt from the payment of income taxes under U. S. Internal Revenue Codes prior to 1942, it does not follow that they have always been exempt from taxation. At the time of the first world war mutual insurance companies such as appellant were subject to a tax of 1% on their policy premiums (Section 504, Revenue Act of 1917, Appendix No. XV, Revenue Act of 1918, Appendix No. XVI). These revenue measures were re-enacted in substantially the same form each year through 1921. For that period such companies were not required to pay income taxes (Appendices Nos. VIII and XVII).

This historical data demonstrates another classic example of a tax in our own Internal Revenue Code that was in effect a tax “in lieu of” or “in place of” an income tax, insofar as it was applied to mutual insurance companies such as appellant.

From 1921 to 1942 various minor changes were made in the exemption of mutual insurance companies

under the U. S. Internal Revenue Code, until in the 1942 amendment the following change was made by Section 165(e) of the 1942 act.

Prior to the 1942 amendment Section 101(11) read as follows:

“(11) Farmers or other mutual hail, cyclone, casualty or fire insurance companies or associations (including inter-insurers and reciprocal underwriters) the income of which is used or held for the purpose of paying losses or expenses.” (Appendix No. XVII)

The 1942 amendment changed said section to read as follows:

“(11) Mutual insurance companies or associations other than life or marine (including inter-insurers and reciprocal underwriters) if the gross amount received during the taxable year from interest, dividends, rents and premiums (including deposits and assessments), does not exceed \$75,000.00.” (Appendix No. XVIII)

This change in our own tax law in 1942 made the larger mutual insurance companies such as appellant subject to income taxation. The exact basis of their taxation will be considered in detail in a later part. For the present it will be sufficient to observe that in 1942 mutual insurance companies such as appellant were made subject to tax under Section 207 I.R.C. at the rate of 1% on their “gross amount of income.”

At this same time in Canada mutual insurance companies such as appellant were paying a tax to the Dominion of Canada in the amount of 3% on “net premiums” which is, in effect, a gross income tax.

What was the intent of Congress in adding subsection (h) to Section 131 I.R.C. in 1942? In said year Congress imposed upon mutual insurance companies such as the appellant a tax under section 207 I.R.C. on a "gross income" basis. Such tax itself was "in lieu of" or "in place of" a "net income tax" of the traditional kind. At the time of levying such tax on such basis on mutual insurance companies such as appellant Congress liberalized the provisions of Section 131 by adding thereto subsection (h) to permit the granting of credit for taxes paid to foreign countries on a similar basis. The tax for which appellant claims a credit is a tax imposed on a similar basis as will be pointed out in the next section. Manifestly, Congress intended that appellant should be allowed a foreign tax credit under these circumstances.

(d)

*The similarity between the basis of appellant's tax under the United States and Canadian laws indicates Congress intended to permit a foreign tax credit under the circumstances of this case.*

Although prior to 1942 appellant was able to qualify for exemption under U. S. tax laws, in that year the U. S. Internal Revenue Code was amended, as previously observed, so as to impose upon appellant an income tax under the provisions of Section 207 I.R.C. Significantly, such section did not impose on appellant the traditional type of income tax. Prior to the 1942 amendment the term "income tax" as employed in U. S. tax law referred only to a "net income tax" imposed upon "profits."

Under the provisions of Section 207 I.R.C., mutual insurance companies such as appellant may be subjected to a tax upon the basis of their "*net investment income*," or they may be subjected to a tax on the basis of their *gross amount of income*. Whichever basis produces the larger tax is the basis that must be used. During 1942 and 1943 appellant actually paid its tax under the provisions of Section 207 on the basis of its gross amount of income. The gross amount of income as defined in that section is composed of net premiums and gross investment income. It is clearly not an "income tax," as that term was used prior to the enactment of the 1942 amendment to Section 207 I.R.C. In fact and in operation it is actually a tax "in lieu of a tax upon income" within the literal meaning of that phrase, if the traditional definition of income tax is employed. Admittedly, the U. S. statute does not specifically refer to such tax as a tax in lieu of a tax upon income. There are no administrative rulings and no court decisions that specifically hold that the alternate tax under Section 207 based upon the gross amount of income of a mutual fire insurance company is a tax in lieu of a tax upon income. Obviously, however, such tax was intended to be a tax in lieu of a tax upon income of such mutual insurance companies according to the standards employed in our own tax law prior to 1942.

The Canadian Special War Revenue Tax for the years 1942 and 1943 provides a perfect analogy. Admittedly, the Canadian law does not specifically state that it is a tax in lieu of a tax upon income. Nor are there any court decisions or administrative rulings



so providing. But in fact and in operation it is as much of a tax in lieu of an income tax of the traditional kind as the tax imposed on appellant under Section 207 I.R.C.

The tax paid by appellant for those years in the United States was virtually a "premium tax" at the rate of 1%. Gross income under Section 207 I.R.C. is composed of net premiums and gross investment income. The relationship between the investment income and net premium income of a general writing insurance company such as appellant may be illustrated by appellant's returns for the years 1942 and 1943 (See Appendix No. XI). During those years appellant's "net premiums" constituted approximately 97% of its *gross amount of income* which, under Section 207 I.R.C., was the basis of its income tax in the United States. Thus, where the taxpayer pays its tax on the basis of the gross amount of income under Section 207 the "net premiums" of the taxpayer constitute by far the largest part of its taxable income. The investment income is an almost negligible factor in the production of taxes payable under the gross amount of income provision of Section 207 I.R.C. Because appellant's taxes for those years was based largely upon its net premiums, for practical purposes it might be said that during those years appellant paid a "net premium tax" in the United States. This included the same "net premiums" of appellant that were taxed as such by the Dominion of Canada. In fact, during 1942 and 1943 appellant's "net premiums" on its Canadian operations in the amounts of \$509,072.00 and \$540,084.67, respectively (as con-

verted from Canadian to U. S. dollars at 90.909%) were, for practical purposes, taxed as such in both Canada and the United States. In the United States the tax was called a "gross amount of income tax." In Canada it was called the Special War Revenue "net premium tax." Appellant contends that what the respective taxes were called is unimportant. Their effect is important. The appellee cannot deny that their effect was to subject appellant's "net premiums" on its Canadian operations to *double taxation*. The appellee cannot deny that the consistent intent of Congress in enacting and amending Section 131 I.R.C. has been to mitigate, as far as possible, the evils of double taxation—to thereby encourage domestic corporations to operate in foreign countries with assurance that their income there will not be taxed again here. The appellee cannot deny that subsection (h), when added to Section 131 I.R.C. by Congress, was added with the express intention of liberalizing the provisions of that section so that it could carry out more effectively that broad general purpose of avoiding double taxation. Indeed the similarity between the basis of appellant's tax under the U. S. and Canadian laws indicates Congress expressly intended to permit a foreign tax credit under the circumstances of this case.

## IV.

**Construing the Special War Revenue Act, as Applied to Mutual Insurance Companies, Such as Appellant, According to the Intent of Parliament Indicates Appellant is Entitled to the Foreign Tax Credit Claimed.**

The Commissioner has denied appellant's foreign tax credit claim because there is no court decision, administrative ruling, or declaration in the Canadian laws that indicates in express terms that the Canadian Special War Revenue Act was intended by Parliament to be a tax in lieu of a tax upon the income of mutual insurance companies such as appellant. Had there been such express provisions this action would never have arisen. Appellant contends that the provisions of Section 131 I.R.C. do not require that a foreign tax, to be allowed as a credit, must be imposed under a law which states expressly that it is a tax "in lieu of" a tax upon income.

While appellant contends that the standard adopted by the Commissioner for determining the allowability of foreign tax credits is too strict, appellee must concede that the intent of the foreign legislative body, in this case Parliament, has some probative value. In the proof of a claim under Section 131(h) I.R.C. the appellee would apparently agree that if the Canadian Parliament intended the Special War Revenue Act as amended in 1942, to serve as a tax "in lieu of" an income tax for mutual insurance companies such as appellant, then the taxes paid by appellant to Canada under the provisions of that law would be taxes for which a credit could be allowed under the provisions of Section 131(h) I.R.C. For that reason

appellant will discuss the facts that tend to establish the intent of Parliament.

(a)

*The early historical background of the Canadian Special War Revenue Act and the Income War Tax Act indicates the Canadian Parliament intended the Special War Revenue Act to serve, during the years of 1942 and 1943, as a tax "in lieu of" an income tax for mutual insurance companies such as appellant.*

Very much like the special excise tax of 1909 in our own law which was enacted prior to any general income tax act, the Canadian Special War Revenue Act of 1915 was enacted prior to any general income tax act in Canada. As previously observed, the U. S. special excise tax of 1909 was a tax of 1% on net income in excess of \$5,000.00. The Special War Revenue Act of 1915 was a tax of 1% on net premiums. As observed, according to the literal meaning of the words the, U. S. special excise tax of 1909 was a tax "in lieu of" an income tax, because it was enacted some four years prior to the passage of a general income tax law in the United States, to serve as a revenue measure until an income tax law could be enacted. In the same sense, according to the literal meaning of the words, the Special War Revenue tax, when first enacted, was a tax "in lieu of" an income tax which was not imposed in Canada until two years later.

It was in 1917 that the Canadian Income War Tax Act was passed, imposing for the first time a general income tax in Canada. The joint stock type of insur-



ance companies operating for profit were subject to taxation under the Canadian Income War Tax Act of 1917, but the mutual type of insurance organizations, such as appellant, were exempt from taxation under the Canadian Income War Tax Act of 1917 (Tr. 28, 29, 52, 53). Insurance companies organized and operating for profit on the joint stock company plan, which were subject to the income tax law, were permitted to deduct, from their income taxes otherwise payable, the amount of tax which they had paid under the Special War Revenue Act of 1915. Section 7 of Part III of the Canadian Income War Tax Act of 1917, read as follows:

“A taxpayer shall be entitled to deduct from the tax that would otherwise be payable by him under this act the amount paid for corresponding periods under the provisions of Parts II and III of the Special War Revenue Act of 1915.”

The significance of this historical data is two-fold. First, it indicates that prior to the enactment of the Canadian Income War Tax Act of 1917 the Canadian Special War Revenue tax of 1915, according to the literal meaning of the phrase, was a “tax in lieu of” an income tax for all insurance companies. Secondly, it indicates that, at the time of the passage of the Canadian Income War Tax Act of 1917, the Special War Revenue tax as imposed upon joint stock companies paying an income tax, was no longer a tax “in lieu of” an income tax. With respect to mutual insurance companies such as appellant, which were exempt from income taxation, the Special War Revenue tax continued to be a tax “in lieu of” an income tax.

As previously observed, during the period 1917 to 1921, in our own tax laws mutual insurance companies such as appellant were subject to a tax of 1% on their premiums, but were not during that period required to pay the general income tax imposed in the United States. As observed, according to the literal meaning of the term, that tax was a tax "in lieu of" an income tax with respect to mutual insurance companies. During that same period in Canada mutual insurance companies such as appellant were subject to a tax of 1% on their net premiums, but were not during such period subject to Canada's general income tax law. According to the literal meaning of the phrase, such Canadian tax was likewise a tax "in lieu of" an income tax with respect to mutual insurance companies.

In our own tax laws the 1% federal premium tax was not imposed after 1921. From 1921 to 1942 mutual insurance companies such as appellant, did not pay federal income taxes in the United States. In Canada the 1% tax on premiums continued to be imposed up to 1942 on all insurance companies, and during said period for mutual insurance companies such as appellant, exempt by law from the Canadian Income Tax, it continued to be, as to such companies, a tax "in lieu of an income tax otherwise generally imposed."

## (b)

*The historical background of the 1942 amendment to The Special War Revenue Act indicates the Canadian Parliament intended it to serve during the years 1942 and 1943 as a tax "in lieu of" an income tax for mutual insurance companies such as appellant.*

From 1917 to 1942 mutual insurance companies such as appellant operating in Canada were exempt from the general income tax law of Canada (Tr. 28, 29, 54, 55). For said period the only equivalent Dominion tax imposed upon such companies was the Special War Revenue tax at the rate of 1% (Tr. 32, 33, 53).

In 1942, as in 1915, Canada was engaged in another war and the need for additional revenue was acute. An increase in all taxes was necessary. Accordingly, at that time the Special War Revenue Act was amended. As applied to insurance companies organized on the joint stock company basis—that is, companies operating for profit (which were subject to the general Canadian income tax and excess profits tax)—the rate of said tax was increased by the 1942 amendment from 1% to 2% (Tr. 32, 33, 54). As applied to insurance companies, such as appellant, organized on the mutual basis—that is, companies not operating for profit (which were not subject to the general Canadian income tax act or the excess profits tax)—the rate of said tax was increased by the 1942 amendment from 1% to 3% (Tr. 33, 34, 54).

At the time of the amendment of the Special War Revenue Act in 1942 no change was made in the provision of the Canadian Income War Tax Act which

exempt mutual insurance companies such as appellant from taxation thereunder (Tr. 28, 37, 54, 55).

In the Parliamentary debates at the time of the adoption of the 1942 amendment to the Special War Revenue Act, Honorable J. L. Ilsley, Minister of Finance, in justification of the apparent discrimination in rates of the proposed amendment pointed out that the higher rates imposed by the proposed amendment were imposed because of advantages in income taxation enjoyed by organizations paying the higher rates under the Special War Revenue Act. A member of Parliament, Mr. Diefenbaker, asked the following question: "Why it it that, for instance, Lloyds are required to pay 3 per cent tax and other companies in the Dominion of Canada 2 per cent, and that every mutual company shall pay to the Minister a tax of 4%? What is the reason for the apparent difference in rates?" While the following statements of the Minister of Finance in response to that specific question did not specifically refer to mutuals, the same controlling purpose behind the rate differential is evident in the case of mutual insurance companies. Obviously, the Minister of Finance intended his remarks to apply to mutuals as well as Lloyds. With respect to the imposition of taxes on them the Hon. Mr. Ilsley (Minister of Finance) stated as follows:

"\* \* \* Therefore you have the competitors of Lloyds paying income tax on a less advantageous basis than Lloyds. We contend that it is fair that Lloyds should pay premium tax on a less advantageous basis than others.

\* \* \* \* \*



“No, my whole argument is that income tax is imposed on Lloyds on a more favorable basis than on their competitors in Canada, and conversely the premium tax is higher on Lloyds than on their competitors.”

See Dominion of Canada, official Report of Debates, House of Commons, Third Session, Ninth Parliament, 6 George VI, Volume V, 1942, July 24, 1942, pages 4643, 4644.

These remarks of the Canadian Minister of Finance at the time of the adoption of the 1942 amendment to the Canadian Special War Revenue Act are significant for two reasons. They indicate that in 1942 Lloyds and mutuals, such as appellant, which were subject to a 3% tax under the Canadian Special War Revenue Act rather than a tax of 2% because they enjoyed an advantage under Canada's general income tax law that was not enjoyed, and could not be enjoyed by the stock insurance companies. Secondly, it indicates that mutual insurance companies such as appellant were subject to a tax at the rate of 3% under the Canadian Special War Revenue Act as amended in 1942, because the advantage they enjoyed was complete exemption from the payment of taxes under the Canadian Income War Tax Act. This differential in rate is thus positive evidence of the fact that the Canadian Parliament intended the Special War Revenue Act to serve, during the years 1942 and 1943, as a tax “in lieu of” an income tax for mutual insurance companies such as appellant.

(c)

*The background of the 1946 amendment to the Special War Revenue Act indicates the Canadian Parliament intended it to serve during the years 1942 and 1943 as a tax "in lieu of" an income tax for mutual insurance companies such as appellant.*

Prior to the 1946 amendment to the Canadian tax laws mutual insurance companies such as appellant were exempt from Canada's general income tax law under Section 4 (g) of the Canadian Income War Tax Act (Tr. 28, 29, 37, 54, 55). By virtue of such exemption appellant was also exempt from taxation under the Canadian Excess Profits Tax Act of 1940. This exemption appeared in the Canadian Income War Tax Acts from its original enactment in 1917 until 1946 (Tr. 35, 36, 54, 55). By the terms of the 1946 amendment to the Canadian Income War Tax Act this exemption was so restricted that beginning with January 1, 1947, general writing mutual fire and casualty insurance companies, including the appellant, were made subject to the general income tax law of Canada (Tr. 35, 36, 54, 55).

After January 1, 1947, corporations operating on the mutual principle (other than insurance corporations) continued to be exempt from the general income tax law, and mutual companies which derived all of their premiums from insurance on churches, schools or other religious, educational or charitable institutions, continued to be exempt, but general writing mutual fire and casualty insurance companies such as appellant on that date became subject to the general income tax law of Canada (Tr. 35, 36, 54).

In 1946 when the exemption from income and excess profits taxes was withdrawn from mutual fire and casualty companies (except those insuring only churches, educational and charitable institutions) Parliament amended the Special War Revenue Act at the same session reducing the premium tax rate on mutual companies from 3% and 4% down to 2% (Tr. 38, 55). The premium tax rate under the Special War Revenue Act since 1946 has been 2% for general writing mutual fire and casualty insurance companies such as appellant, as well as for stock insurance companies (Tr. 38, 54, 55). This was accomplished by amending Section 14 of the Special War Revenue Act, so that Section 14 (1) was made applicable to general writing mutual fire and casualty companies such as appellant (Tr. 37, 38, 55). At the same time Section 14 (2) was amended to apply to Lloyds and reciprocal exchanges only and provided for the levy of a tax at the rate of 3% on such insurance organizations. Section 14 (3) was repealed by the 1946 amendment.

Parliament made the changes in the Special War Revenue Act in 1946 in accordance with the budget resolution presented to Parliament by the Minister of Finance speaking for the administration. In presenting the budget resolution to the House of Commons the Honorable Douglas Abbott (Acting Minister of Finance) in explaining the proposed reduction in rate from 3% to 2% as applied to general writing mutual insurance companies stated as follows:

“In view of the fact that these mutual insurance companies will no longer be completely exempt from tax, a reduction is being proposed in



the premium tax under the Special War Revenue Act applying to these companies.” (Appendix No. XXV)

As observed, the 1946 amendment preserved a differential in rate in the taxes it imposed. While stock and general writing mutual insurance companies were taxed at the rate of 2% Lloyds and reciprocal exchanges were taxed at the rate of 3%. In presenting the budget resolution the Honorable Mr. Abbott in explanation of this rate differential stated as follows:

“These two classes, it is believed, will not be subject to corporation income tax in Canada, and because of this fact the premium tax in their case will be 3% in place of the general 2%.” (Appendix No. XXV)

These pertinent comments, together with the comments of Mr. Abbott in the House of Commons and the Honorable Messrs. Hayden and Euler in the Senate (set forth in Appendix No. XXV) indicate: (1) that up to 1946 the Special War Revenue Tax was the “principal tax” imposed by the Dominion of Canada upon mutual insurance companies such as appellant; (2) that prior to 1946 the income of mutual insurance companies was “reached through the medium of a tax on premiums”; (3) that “the tax on premiums was practically the same in amount as an income tax on them would have been”; (4) that they were not subject to the corporation income tax in Canada, “and because of this fact” the premium tax in the case of such mutual companies was 3% in place of the general 2%.

Thus, with respect to mutual insurance companies



such as appellant the Special War Revenue Act was in fact, and was intended by Parliament to be, a tax "in place of" or "in lieu of" an income tax on such companies in 1942 and 1943.

## V.

### **The Applicable Rulings by the Commissioner of Internal Revenue Indicate That the Appellant Is Entitled to the Foreign Tax Credit Claimed**

#### (a)

*The Commissioner's rulings prior to 1942 indicate appellant is entitled to the foreign tax credit claimed.*

An examination of the Commissioner's rulings construing the foreign tax credit provisions of the U. S. Revenue Acts from 1917 to date indicates that these rulings have been based upon the same test to determine whether or not the foreign tax credit should be allowed. No substantial change has taken place since the addition of subsection (h) to Section 131 I.R.C. in 1942.

An analysis of the pertinent rulings construing the foreign tax credit provisions of the Revenue Acts from 1917 to 1942 indicates that the foreign tax credit has been allowed whenever the foreign tax under consideration was based upon profit or "income" as that term was understood and employed in United States tax laws. They indicate that the concept of "income" as the term was understood in our tax laws up to 1942 was a gain derived from the employment of labor or capital or both. I.T. 2620 XI-1, C.B. 44 (See Appendix No. XX for additional rulings).

An analysis of the Commissioner's rulings between

1917 and 1942 in which the foreign tax credit was denied leads to two general conclusions. First, that a foreign tax that did not obviously qualify as a tax on "income" within the concept of that term as it was used and recognized in the United States income tax law was not allowed as a credit. I.T. 1444, I-2, C.B. 168, I.T. 2909, XIV-2, C.B. 136 (See Appendix No. XXI for additional rulings).

Secondly, it leads to the conclusion that there has been an observable tendency on the part of the Commissioner to construe the foreign tax credit provisions of the various revenue acts more strictly, rather than more liberally. Compare I.T. 2070, III-2, C.B. 250 and I.T. 2909, XIV-2, C.B. 136; *United States Fidelity & Guaranty Co. v. Commissioner* (1926) 5 B.T.A. 23 and I.T. 3138, 1937-2, C.B. 230 (See Appendices Nos. XX, XXI).

Of the foregoing rulings the one that is particularly pertinent in the instant case is I.T. 3138, 1937-2, C.B. 230. In construing the foreign tax credit provisions of the Revenue Acts of 1932 and 1934 the Commissioner ruled that the 1% premium tax imposed by the Canadian Special War Revenue Act could not be allowed as a foreign tax credit. Considering this particular decision in its proper setting supports appellant's contention that it is entitled to the foreign tax credits claimed.

Prior to this ruling taxpayers had been permitted to claim the Canadian Special War Revenue Tax as a foreign tax credit. See *United States Fidelity and Guaranty Co. v. Commissioner* (1926) 5 B.T.A. 23 and the discussion of Internal Revenue Department

policy in *St. Paul Fire & Marine Insurance Co. v. Reynolds* (1942) 44 F. Supp. 863, 865, 29 A.F.T.R. 592. This ruling therefore, represented a change in the Commissioner's policy with respect to this particular tax, and a change toward a more strict construction of the foreign tax credit provisions of our own Revenue Acts.

The reasoning that led to the conclusion set forth in this ruling should be considered. First, the familiar test was applied to determine whether or not the tax was a tax on "income" within the concept of that term as used in the U. S. tax law. In applying the test to the facts the Commissioner observed that the tax was imposed under the provisions of the Special War Revenue Act which in name, at least, was separate and distinct from the Canadian Income Tax Act. The Commissioner further observed that the tax was imposed on the net premiums of the taxpayer without regard to whether or not a gain or net profit was realized therefrom. That decision was based to some extent upon the fact that the deductions permitted under the Special War Revenue Act were completely unrelated to the deductions permitted under U. S. Income Tax Laws. On that basis and because premium taxes were generally regarded as excise or privilege taxes the Commissioner concluded that the Special War Revenue tax was not a tax on income as the term was understood and used in our tax laws up to that time and for that reason could not be allowed as a foreign tax credit.

That Commissioner's ruling is of interest not only because of the line of reasoning upon which it was



based, but also because of the fact that it was affirmed by the Board of Tax Appeals in the case of *Continental Insurance Company v. Commissioner* (Sept. 9, 1939) 40 B.T.A. 540, and by the United States District Court in the case of *St. Paul Fire & Marine Insurance Company v. Reynolds* (March 9, 1942) 44 F. Supp. 863, 29 A.F.T.R. 592, which as previously indicated was decided just a little more than six months before the adoption of the 1942 amendment adding subsection (h) to Section 131 I.R.C.

An analysis of all of the Commissioner's rulings leads to the conclusion that prior to the addition of subsection (h) to Section 131 I.R.C. a foreign tax would not be allowed as a foreign tax credit if: (1) it was a tax based upon gross receipts, gross sales, or gross revenue; (2) it was a tax imposed without regard to whether or not a gain or profit was realized; (3) it was imposed under a statute which was not a part of the general income tax act of the foreign country imposing the tax. This represents in general terms the effect of the Internal Revenue Department rulings immediately prior to the addition of subsection (h) to Section 131 I.R.C.

As previously indicated herein the 1942 amendments to the Internal Revenue Code made at least two major changes in the previous Revenue Act. First, the 1942 amendment to Section 207 made provision for imposing on mutual fire insurance companies, such as the appellant, a tax without regard to whether or not a gain or profit was realized, on the basis of gross amount of income (net premiums plus gross investment income). Secondly, the 1942



amendment extended the foreign tax credit provisions of Section 131 by the addition of subsection (h).

As previously observed in Part III(b) *supra*, at the time of the addition of subsection (h) to Section 131 I.R.C. in 1942, and in regard to the broadening of the foreign tax credit provisions of that section, the Committee on Finance of the Senate stated:

“\* \* \* In the interpretation of the term ‘income tax’ the Commissioner, the Board and the Courts have consistently adhered to a concept of income tax rather closely related to our own, and if such foreign tax was not imposed upon a basis corresponding approximately to net income it was not recognized as a basis for such credit. Thus if a foreign country in imposing income taxation authorized \* \* \* a United States domestic corporation doing business in such country to pay a tax in lieu of such income tax but measured for example by gross income, gross sales or a number of units produced within the country, such tax has not heretofore been recognized as a basis for credit. Your Committee has deemed it desirable to extend the scope of this section \* \* \*.”

This quotation is repeated here to emphasize the fact that:

(1) Congress was cognizant of the Commissioner’s rulings referred to and was familiar with the line of reason upon which they were based; (2) Congress intended to liberalize or “extend the scope” of the foreign tax credit provisions of the Code; (3) Congress specifically intended to change the foreign tax credit test that prior to the 1942 amendment had required that the foreign tax must be imposed upon

substantially a net income basis before it could be allowed as a foreign tax credit; (4) Congress specifically intended that a foreign tax based upon gross income, such as the Special War Revenue tax should not be disallowed as a foreign tax credit for that reason.

(b)

*The Commissioner's rulings since 1942 indicate appellant is entitled to the foreign tax credit claimed.*

An examination of the Commissioner's rulings since the enactment of the 1942 amendment should indicate why the Commissioner and the Tax Court have wrongfully denied appellant a foreign tax credit to which it is entitled.

An analysis of the pertinent rulings construing the foreign tax credit provisions of the Internal Revenue Code from 1942 to date indicates that the Commissioner is employing, without change, the same test that was employed prior to the amendment of Section 207 I.R.C., and prior to the addition of subsection (h) to Section 131 I.R.C. in 1942. They indicate that the foreign tax credit has been allowed only when the foreign tax was placed upon profit or "income" as that term was understood and employed in United States tax laws prior to 1942. I. T. 3778, 1946-1, C.B. 11 (See also Appendix No. XXII for additional rulings).

Perhaps the Commissioner's ruling in I. T. 3903, 1948-8, C.B. 5, would seem to be an exception to the rule. It is not. There the Commissioner ruled that a 3% Cuban tax on the gross revenues received from

freight and passengers taken aboard in Cuban ports by foreign shipping companies was a tax for which a foreign tax credit would be allowed under Section 131(h) I.R.C. Allowing the credit under the provisions of subsection (h) of Section 131 is the only revolutionary part of the rulings. The Cuban tax under consideration is an additional tax imposed under the same tax statute that was the subject of the Commissioner's ruling in I. T. 2596, X-2, C.B. 184 (See Appendix No. XXI, page A-22) in which, construing the foreign tax credit provisions of the Revenue Act of 1928, the Commissioner ruled that the tax was an excise tax and that it could not be allowed as a foreign tax credit. The earlier ruling was nullified, however, by the Board of Tax Appeals in the case of *Seatrains Lines Inc. v. Commissioner* (1942) 46 B.T.A. 1076. That ruling, therefore, merely represents the Commissioner's confirmation of the decision of the Board of Tax Appeals in the *Seatrains* case, *supra*, and a ruling that the tax in question should be allowed as a foreign tax credit under the provisions of the new subsection (h) of Section 131. In the *Seatrains* case, *supra*, it was held that a similar tax imposed under the same law could be allowed as a credit under the provisions of Section 131(a)(1) of the Revenue Act of 1936 which is carried over into the present revenue act.

Since the addition of subsection (h) to Section 131 I.R.C., in 1942, there has been only one ruling that a foreign tax could not be claimed as a credit under Section 131 as amended. An Ecuador contribution tax of 5% on net profits of employers was disallowed as a



foreign tax credit. I.T. 3768, 1945 C.B. 204. That tax was imposed for the specific purpose of providing numerous benefits for employees under the labor code of Ecuador. The Commissioner's ruling was based upon the conclusion that the tax was not a "tax" as the term is generally understood, but was rather an imposition for the purpose of regulating certain industries or businesses and that it was not for the purpose of raising revenue for the general support of the government.

These are the pertinent rulings that have been published since the addition of subsection (h) to Section 131 I.R.C. in 1942. The Commissioner's ruling in the instant case has not been published, but it is apparent that in this case the Commissioner's ruling follows the pattern of the rulings issued both prior and subsequent to the 1942 amendment.

(c)

***Applying the Commissioner's own test indicates appellant is entitled to the foreign tax credit claimed.***

The Commissioner has denied appellant's foreign tax credit in this case because in the Commissioner's opinion the Canadian tax in question is not a tax on "income" as that term was understood in the United States tax laws prior to 1942. What the Commissioner's ruling in this case ignores is fundamental. It ignores the admitted fact that the concept of an "income tax" as the term is used in the Internal Revenue Code changed considerably with the enactment of the 1942 amendments to Section 207 and Section 101 (11) (See Appendices Nos. II and XVIII).



It is for that reason that it is appellant's contention that the Commissioner's rulings indicate that appellant is entitled to the foreign tax credits claimed. For the purpose of elucidating appellant's contention let us apply the Commissioner's test to the Canadian tax in question, noting, however, that the concept of an "income tax" as the term is used in the United States Internal Revenue Code has changed fundamentally with the amendment of Section 207 I.R.C. in 1942. What are the facts with respect to the "income tax" imposed by our Code upon mutual fire insurance companies such as the appellant after 1942? As previously pointed out in a preceding part our own "income tax" on mutual fire insurance companies imposed under Section 207 I.R.C. as amended in 1942 indicates:

- (1) The alternate tax is based upon *gross amount of income*, which consists very largely of "*net premiums*."
- (2) The alternate tax is not a tax imposed upon "profit" or "income" from the employment of capital or labor or both as that term was used and understood in our tax law prior to 1942.
- (3) The alternate tax paid by appellant is imposed upon its "net premiums" and "gross investment income" irrespective of whether or not a profit is realized.

As mentioned in a preceding part a drastic change was made in the concept of "income tax" as that term had previously been understood in our tax law. Prior to the 1942 amendment foreign taxes were disallowed as foreign tax credits when found to possess any one of the above characteristics because the tax was not

a tax on income as that term was understood and employed in the U. S. tax law.

What are the characteristics of the Canadian Special War Revenue tax for which the foreign tax credits are claimed? The Canadian taxes possess the same general characteristics as the tax paid by the appellant under the alternate tax provisions of Section 207 I.R.C. as amended in 1942.

Prior to the 1942 amendment the tax could have been disallowed and would have been disallowed as a foreign tax credit if found to possess any one or more of these characteristics<sup>is</sup>. The reason for the disallowance of a similar tax as a foreign tax credit in I. T. 3138, 1937-2, C.B. 230 (Appendix No. XXI) was that the Canadian tax was not a tax on income as that term was understood and employed in the U. S. tax law. The Commissioner's ruling in this case was based upon the same reason. Such reason ignores the facts.

This indicates that a proper application of the Commissioner's own test regarding the granting or denial of foreign tax credits, if interpreted in light of the 1942 amendment, will indicate that appellant should be allowed the foreign tax credit claimed.

Assume that in 1942 Congress did not intend to change the fundamental concept of an "income tax" as that term had been understood and used in our tax laws prior thereto. The conclusion is inescapable that appellant is entitled to the foreign tax credit claimed.

Assume that an "income tax" must still be a tax on profit or on the gain from the employment of capi-

tal or labor or both. Assume that this is the standard by which foreign taxes must be measured. Measured by this standard it is clear that the alternate tax imposed on the appellant by Section 207 I.R.C., as amended in 1942, is *not* an "income tax." If such tax is not an "income tax" it certainly is "a tax paid in lieu of a tax on income" as that phrase is employed in subsection (h) of Section 131 I.R.C., which was also added by amendment in 1942. This is true even though our tax law does not specifically state that it is "a tax in lieu of a tax on income," and in spite of the fact that there are no administrative rulings, or court decisions so holding.

Assume then, that the Canadian Special War Revenue Tax is not an "income tax" as that term is understood and used in the U. S. Internal Revenue Code. The conclusion is inescapable that such tax is "a tax in lieu of a tax on income" as that phrase is employed in subsection (h) of Section 131 I.R.C. The similarity between the U. S. and Canadian taxes has been previously discussed. Both are based largely on "net premiums," both are imposed irrespective of whether a gain or profit is realized; both were imposed as war revenue measures to increase the general revenue of the respective governments to support the war effort; both are imposed when in fact the taxpayer does not pay a tax under the general income tax provisions applicable to other corporations. The fact that both in Canada and the United States there is no specific reference to the tax as "a tax in lieu of a tax on income" either in the law, the administrative rulings or the decisions of the court lends support to

appellant's contention that if the one is an "in lieu of tax" the other must be.

For that reason the Commissioner's own test indicates appellant is entitled to the foreign tax credit claimed. The Commissioner's rulings, as pointed out in this part, support appellant's claim.

## VI.

### **The Applicable Case Law Indicates Appellant Is Entitled to the Foreign Tax Credit Claimed.**

#### (a)

*The historical background of the cases dealing with the Canadian Special War Revenue Tax as a permissible foreign tax credit indicates appellant is entitled to the foreign tax credit claimed.*

From the decision of the Federal District Court in the case of *St. Paul Fire & Marine Insurance Company v. Reynolds* (1942) 44 F. Supp. 863, 866, 29 A.F.T.R. 592, it appears that from 1918 until 1926, during which period there was no case law on the subject, the Commissioner allowed the Canadian Special War Revenue tax as a credit against taxpayers U. S. income tax. In 1926 in the earliest case law in which the question was raised, the Canadian Special War Revenue tax was conceded to be an income tax within the purview of Section 38 of the Revenue Act of 1918.

*U. S. Fidelity & Guaranty Company v. Commissioner* (1926) 5 B.T.A. 23.

The fact that for the purposes of that case the Commissioner conceded that the Special War Revenue



Tax of 1% on premiums paid to the Dominion of Canada was an income tax indicates that from 1918 to 1926 the Canadian Special War Revenue Tax was consistently allowed by the Commissioner as a foreign tax credit.

The Commissioner's practice from 1926 to 1937 is obscure, there being no printed regulations dealing specifically with the Canadian Special War Revenue Tax. Presumably, the long recognized practice of allowing it as a foreign tax credit continued up to 1937. That such was the case seems evident. During most of that period appellant was the owner of the Northwest Casualty Company, a stock casualty company, which operated in both Canada and the United States. In the Commissioner's field audit of that company's U. S. income tax return as late as January 20, 1936, D. M. Kirby, Internal Revenue Agent, on behalf of the Commissioner stated, respecting the Canadian Special War Revenue Tax, the following:

"The taxpayer was subject to the tax on gross revenue levied for 1934, by the Dominion of Canada under the Special War Revenue Act in the amount of \* \* \*.

"This tax has been held to be an income tax (5 B.T.A. 23) and in prior years has been claimed as a credit for income taxes paid to a foreign country \* \* \*."

In 1937 in I.T. 3138, 1937-2, C.B. 230 (Appendix No. XXI), the Commissioner ruled that under Section 131 of the Revenue Acts of 1932 and 1934 the Canadian Special War Revenue Tax of 1% on net premiums could not be allowed as a foreign tax credit.

The question of allowing the Special War Revenue Tax as a foreign tax credit was not again litigated until in 1939 the Board of Tax Appeals case of *Queen Insurance Company of America v. Commissioner* (August 18, 1939), 40 B.T.A. 484. In that case the Board of Tax Appeals held that where the Canadian Income War Tax Act provided that the taxpayer could deduct from the amount of income tax otherwise due the amount of premium taxes paid under the Special War Revenue Act, the taxpayer was entitled to claim the full amount of the income tax (including that portion actually paid as Special War Revenue taxes) as a foreign tax credit under the provisions of Section 131(a)(1) I.R.C. This constituted a holding that the Canadian Special War Revenue Tax could be indirectly allowed as a foreign tax credit under Section 131(a)(1) I.R.C. That case was soon followed by the case of *Continental Insurance Company v. Commissioner* (Sept. 9, 1939) 40 B.T.A. 540. Following the decision of the Board of Tax Appeals in the *Queen Insurance Company* case, *supra*, the Board held in that case that the total amount of income taxes due under the Canadian Income War Tax Act, including the amount of tax credited but originally paid as a premium tax under the Special War Revenue Act, was a proper credit under the provisions of Section 131(a)(1) I.R.C. In that case, however, there were two companies whose premium taxes under the Canadian Special War Revenue Act had exceeded the amount of their income taxes due under the provisions of the Canadian Income War Tax Act. With respect to these companies the board was called upon

to specifically decide whether or not the Canadian Special War Revenue Tax was an income tax for which a credit could be allowed under the provisions of Section 131(a)(1). The board concluded that the Canadian Special War Revenue Tax was not an "income tax" within the meaning of that term as used in the Internal Revenue Code and held for that reason it could not be allowed as a foreign tax credit under Section 131(a)(1) I.R.C. The net effect of the decision of the board in that case was to hold that the Canadian Special War Revenue Tax could be allowed indirectly but not directly, as a foreign tax credit under Section 131(a)(1) I.R.C. It altered somewhat the effect of its decision in the case of *U. S. Fidelity & Guaranty Company, supra*. It confirmed in part and rejected in part the Commissioner's ruling in I.T. 3138, 1937-2, C.B. 230 (Appendix No. XXI).

An appeal was taken from the Board's decision in the case of *Queen Insurance Company of America v. Commissioner, supra*. The decision of the Board in that case was reversed by the Circuit Court of Appeals in the case of *Helvering v. Queen Insurance Company* (1940) 115 F.(2d) 341, 25 A.F.T.R. 996. The decision of the court in that case is not very enlightening because of its brevity. It held that the taxpayer could claim a foreign tax credit under the provisions of Section 131(a)(1) I.R.C., only for the amount of tax actually paid as income tax under the provisions of the Canadian Income War Tax Act. The court held this did not include the amount deducted by the taxpayer from its Canadian income tax for the Special War Revenue Tax which it had paid. In that case the tax-



payer had conceded that the Canadian Special War Revenue Tax, as such, could not be allowed as a foreign tax credit under the provisions of Section 131(a)(1) I.R.C. That case confirmed in part and overruled in part the board's decision in the case of *Continental Insurance Company v. Commissioner, supra*. It was not until 1940 that the case law dealing with the Canadian Special War Revenue Tax held that such tax could not be allowed indirectly as a foreign tax credit under the Internal Revenue Code.

Two years later a Federal District Court in Minnesota decided the case of *St. Paul Fire & Marine Insurance Co. v. Reynolds* (March 9, 1942) 44 F. Supp. 863, 29 A.F.T.R. 592. In that case for the first time it was unequivocally held that the Canadian Special War Revenue Tax could not be allowed either directly or indirectly as a foreign tax credit under Section 131(a)(1) of the Revenue Acts of 1932 and 1934. Since the decision of the court in that case there have been no further cases dealing with the Canadian Special War Revenue Tax as a tax credit. This historical data is most significant. It indicates that from 1918 to 1937 the practice of the Commissioner and the courts was to allow the Canadian Special War Revenue Tax as a credit against taxpayers' United States income tax. From 1937 to 1939 the Canadian Special War Revenue Tax was not allowed as a foreign tax credit because of a ruling of the Commissioner. The issue was not then settled. From 1939 to the decision of the Circuit Court in the case of *Helvering v. Queen Insurance Company* in 1940 the Canadian Special War Revenue Tax was *indirectly* allowed as a foreign



tax credit under Section 131(a)(1). It was not until March 9, 1942, that the case law on the subject definitely established that the Canadian Special War Revenue Tax could not be allowed either directly or indirectly as a foreign tax credit.

As previously indicated herein, less than seven months after a Federal District Court, for the first time, had unequivocally held that the Canadian Special War Revenue Tax could not be allowed, either directly or indirectly, as a foreign tax credit under Section 131(a)(1), the Senate Finance Committee sired the amendment that added subsection (h) to Section 131 I.R.C. The expression of purpose of the Committee quoted at length in previous parts of appellant's brief indicates Congress intended to repudiate the basis of the court's decision in the case of *St. Paul Fire & Marine Insurance Company v. Reynolds*, *supra*. As previously indicated, Congress must be presumed to have intended to change, not only the statutory, but also the case law interpreting it (Citation of Authorities at pages 29, 30). In 1942 Congress knew that between 1940 and 1942 the courts had construed the foreign tax credit provision of the Internal Revenue Code so strictly that they were thwarting its salutary purpose. Subsection (h) was accordingly added to Section 131 I.R.C., to remedy that situation. The Congressional committee which sired the amendment which added subsection (h) to Section 131, likewise sired the amendment to Section 207, making mutual insurance companies, such as appellant, subject to tax on a gross income basis. While Section 207 was added to raise additional revenue,

subsection (h) was added to Section 131, to give to taxpayers such as appellant, which were taxed in foreign countries on a gross income basis, greater, not less, relief from the oppressive burden of foreign taxation. *Burnet v. Chicago Portrait Company* (1932) 285 U.S. 1, 15, 76 L. ed. 587, 594, 10 A.F.T.R. 800.

(b)

*The standards and tests employed by the Courts in those cases in which the Special War Revenue Tax was denied as a foreign tax credit indicate appellant is entitled to the foreign tax credit claimed.*

In construing the foreign tax credit provisions of U. S. Revenue acts prior to 1942 the term "income tax" as used therein was construed to mean a tax on income as that term was used and understood in U. S. tax law. In 1942 at the time of the addition of subsection (h) to Section 131 I.R.C., to be allowed as a foreign tax credit the foreign tax had to qualify as a tax on "income" as that term was understood and employed in the U. S. tax law.

*Biddle v. Commissioner* (1938) 302 U.S. 573, 82 L. ed. 431, 58 S. Ct. 379, 19 A.F.T.R. 1253;

*St. Paul Fire & Marine Insurance Co. v. Reynolds* (1942) 44 F. Supp. 863, 865, 29 A.F.T.R. 592.

A succinct digest of reported cases construing foreign tax credit provisions of the Internal Revenue Code will be found in Appendices Nos. XXIII and XXIV. An analysis of those cases indicates that "income tax" as that term was employed in the U. S. tax

laws prior to 1942 was a direct tax on "income." The term "income" as employed in U. S. tax law prior to the amendment of Section 207 in 1942 was uniformly restricted to a gain realized or a profit derived from capital, labor or both. As observed, from 1940 up to the addition of subsection (h) to Section 131 in 1942 this test was applied by the courts with strictness, and unless the foreign tax under consideration clearly constituted a net income tax on "profits" it was not allowed as a foreign tax credit.

In 1942 the amendment of Section 131(h) and Section 207 made fundamental changes in the U. S. tax law. At that time Congress either intended to approve or repudiate the foreign tax credit test that had been previously employed by the courts. In either event appellant is entitled to the foreign tax credit claimed. If this test is properly employed in this case it must be recognized that the term "income tax" as that term is understood and used in U. S. tax law changed with the 1942 amendment to Section 207. Now the term "income tax" as understood in U. S. tax law may include a tax on gross amount of income as well as "net income." In the application of the test, if cognizance is taken of this fact and the test is strictly applied as it was prior to 1942 it is clear, as previously indicated, that the taxes paid in the United States by appellant under the provisions of Section 207 on the gross amount of income are not "income taxes." If they are not "income taxes" within the meaning of the U. S. tax law they must be taxes paid in lieu of an income tax otherwise generally imposed within the meaning of Section 131(h). For the same reason,



where it appears as it does in this case that appellant, in Canada, did not pay the ordinary type of "net income tax," but instead paid substantially a gross income tax on net premiums under the Special War Revenue Act the Canadian tax constitutes a tax in lieu of an income tax otherwise generally imposed. That is true if the former test is strictly applied.

If the former test is properly applied appellant is entitled to a foreign tax credit under the provisions of either subsection (a) (1) or subsection (h) of Section 131.

In previous parts the similarity between the basis of appellant's tax in the United States and Canada for the year 1942 was discussed. In both countries for that period appellant was taxed on substantially a gross income basis without regard to whether or not appellant had earned a profit in either Canada or the United States. On June 1, 1948, the Second Circuit Court of Appeals decided the case of *New York & Honduras Rosario Mining Co. v. Commissioner* (1948) 168 F.(2d) 745, 747, 36 A.F.T.R. 1115. In that case appellant taxpayer was claiming foreign tax credits under the provisions of Section 131(a) (1) for the years 1941 and 1942. The tax for which appellant claimed credit was substantially a gross income tax imposed by the Republic of Honduras. The Tax Court had denied appellant's foreign tax credit claim on the ground that the Honduras tax was an excise tax. In overruling the decision of the Tax Court the Court of Appeals stated:

"Hence, the ultimate question for determination is whether the foreign tax is the *substantial*



*equivalent* of an ‘income tax’ as that term is understood in the United States.” (Italics ours)

The basis on which this appellant was taxed in 1942 under our own tax law cannot be ignored. Because, the tax paid by appellant to Canada was “substantially equivalent” to the income tax appellant paid in the United States it would qualify the appellant for the foreign tax credit claimed under the provisions of Section 131(a)(1) I.R.C.

Appellant did not choose to claim the foreign tax credit under that section. Appellant claimed its foreign tax credit under the provisions of Section 131(h) because subsection (h) was added to Section 131 in 1942 by the same Congress that subjected appellant, in the United States, to a gross amount of income tax under Section 207 I.R.C. The very close relationship between these amendments in fact and in point of time indicate that Congress was cognizant of the fact that where mutual insurance companies such as appellant paid their tax on the “gross amount of income” basis they were not paying an “income tax” within the meaning of that phrase as it had been previously understood in the U. S. tax law. Congress for that reason specifically intended that if any foreign country should impose upon mutual insurance companies or any other organization a tax on a similar basis it should be allowed as a foreign tax credit as a tax “in lieu of” a tax on “income” as that term had theretofore been understood. Because the tax for which appellant claims credit is a tax imposed by a foreign country on a basis similar to its basis of tax under Section 207 I.R.C., it is precisely the kind of tax that

Congress intended to allow as a foreign tax credit under Section 131(h) I.R.C.

(c)

*The pertinent cases decided since 1942 indicate appellant is entitled to the foreign tax credit claimed.*

Since the amendment in 1942 to Section 131 I.R.C. and Section 207 I.R.C. the only pertinent cases construing the provisions of Section 131 I.R.C. are the United States Court of Appeals case of *New York & Honduras Rosario Mining Co. v. Commissioner* (1948) 168 F.(2d) 745, 36 A.F.T.R. 1115, and the decision of the Tax Court in this case referring to it.

In its decision in this case the Tax Court sought to distinguish appellant's case from the case of *New York & Honduras Rosario Mining Co. v. Commissioner*, supra, solely on the ground that the latter case involved a credit claimed under Section 131(a)(1) and held that the foreign tax credit claimed should be allowed because the foreign tax was "an income tax" within the meaning of that section. That case should not have been disposed of by the Tax Court so summarily. In fact it supports appellant's case.

In that case, for the years 1941 and 1942 the taxpayer had claimed a foreign tax credit under the provisions of Section 131(a)(1) for taxes paid to the Republic of Honduras at the rate of 7% of its liquid profits from the exploitation of mines in that country. On June 23, 1947, the Tax Court in its decision reported in 8 T.C. 1232 denied the foreign tax credits claimed by the taxpayer. In its decision the Tax Court had held that the Honduras tax was an "excise tax"

imposed upon the privilege of exploiting the mining properties within that country, and for that reason were not "income taxes" within the meaning of Section 131(a)(1) I.R.C. In that case the Tax Court denied the taxpayers' foreign tax credits for the same reasons that the Tax Court denied the foreign tax credits claimed by appellant in this case. As previously observed, the United States Court of Appeals (2d Circuit) in that case reversed the decision of the Tax Court and allowed the taxpayer the foreign tax credits claimed under the provisions of Section 131(a)(1) I.R.C. The test employed by the court in that case has already been mentioned. In applying that test the court in that case observed that the purpose of Section 131(a)(1) was to "mitigate the evil of double taxation of domestic corporations on income derived from foreign sources." Citing the case of *Flint v. Stone Tracy Company* (1911) 220 U.S. 107, 145, 31 S. Ct. 342, 55 L. ed. 389, 3 A.F.T.R. 2834, the court stated that what a tax is called does not determine whether it is an income tax or an excise tax. The court observed that it was significant that in Honduras law genuine excise taxes were levied which provided for a forfeiture of the mining company's franchise for failure to pay such taxes, but that with respect to the tax for which a foreign tax credit was claimed there were no forfeiture provisions for non-payment. Conceding that the Honduras tax differed from our federal income tax the court concluded that that did not change its character as an income tax. In reversing the decision of the Tax Court Judge Swan, who wrote the opinion for the court, stated:



“Those debits we hold were payments of income taxes to a foreign country. To hold otherwise would defeat the purpose of Section 131, which was to encourage domestic corporations to do business abroad without having to operate through a foreign corporation, the inducement being that their income from operations abroad should be taxed only once.”

The same compelling reasons exist in this case as in that for the allowance of the foreign tax credit claimed. In this case as in that one in the foreign law which imposed the tax for which a credit is claimed there is no forfeiture provision for the non-payment of such tax (Appendix No. XXVI). In this case, as in that one to deny the appellant taxpayer the foreign tax credit claimed would thwart the salutary purpose of Section 131 I.R.C. by subjecting appellant taxpayer to double taxation on its income from foreign operations.

The most recent case construing the provisions of Section 131 I.R.C. is the decision of the Tax Court in the case from which this appeal is taken. It is the only case which so far has attempted to construe the provisions of subsection (h) of Section 131 I.R.C. In its decision the Tax Court concluded that appellant could not be allowed the foreign tax credits claimed because the tax paid by it was not a tax “in lieu of an income tax otherwise generally imposed” within the meaning of subsection (h) of Section 131 I.R.C. It concluded that the tax was not a tax “in lieu of an income tax otherwise generally imposed” because: (1) The Special War Revenue Tax was enacted prior to the Canadian Income War Tax Act; (2) In 1946



when appellant became subject to taxation under the Canadian Income War Tax Act the Special War Revenue tax on premiums was not removed; (3) Prior to the enactment of subsection (h), *supra*, it had been held that the Canadian premium tax was not an income tax within the meaning of Section 131(a)(1) of the revenue acts of 1932 and 1934, which was similar to Section 131(a)(1) I.R.C. of 1942 and 1943. Citing the cases of *St. Paul Fire & Marine Insurance Co. v. Reynolds*, *supra*; *Continental Insurance Co. v. Commissioner*, *supra*, and *Helvering v. Queen Insurance Co.*, *supra*, the Tax Court concluded that the tax for which appellant claimed a foreign tax credit was an "excise tax," and for that reason could not be allowed as a foreign tax credit under Section 131(h) I.R.C.

Each one of the reasons upon which the Tax Court based its decision in this case is a plausible reason why the appellant is entitled to the foreign tax credit claimed.

(1) *The Special War Revenue Tax was enacted prior to the Canadian Income War Tax Act.* This is the strongest kind of evidence that at that time the Special War Revenue Tax was a tax "in lieu of an income tax" for all insurance companies to which it applied. The formulation of a satisfactory net income tax law is an intricate and difficult undertaking. The formulation and collection of a gross income tax is comparatively simple. As previously observed, in our own law all insurance companies and business corporations were subjected to a gross income tax under the special excise tax law of 1909 (36 Stat. at L. 11, 112—117, ch. 6 U.S. Comp. Stat. Supp. 1909, pages

659, 844, 849) before the enactment of a general net income tax law. As previously observed, when a general net income tax law was enacted in Canada as in the United States, mutual insurance companies such as appellant were not subject to taxation thereunder. But in Canada, at the time of the adoption of the Income War Tax Act in 1917, the Special War Revenue Tax was continued with respect to insurance companies operating for profit as joint stock companies. The Income War Tax Act, however, provided that such companies could deduct from the amount of their net income tax otherwise payable the amount of tax they had paid under the Special War Revenue Tax. As previously observed, up to 1940 such companies were thus able to indirectly claim the Special War Revenue Tax as a foreign tax credit as an income tax paid to a foreign country. Not being subject to the general income tax law of either Canada or the United States during that period, mutual insurance companies operating in Canada, paid the Special War Revenue Tax during that entire period as a tax "in lieu of an income tax" within the literal meaning of that phrase. The 1942 amendment to the Canadian Special War Revenue Act did not change its character. So far as mutual insurance companies were concerned it always had been a tax "in lieu of" an income tax. After 1942 it continued to be a tax "in lieu of" an income tax for mutual insurance companies such as appellant.

(2) *In 1946 when appellant became subject to the Canadian Income War Tax Act the Special War Revenue Tax on premiums was not removed. That is un-*

disputed. Appellant is not contending, however, that the Canadian Special War Revenue Tax is a tax "in lieu of an income tax" in the year 1946. In the year 1946, appellant became subject to tax in the Dominion of Canada under both the Canadian Income War Tax Act and the Special War Revenue Act on the same basis as stock insurance companies and other organizations paying income taxes. For taxes paid to Canada after 1946, appellant will be able to claim foreign tax credits under the provisions of Section 131(a)(1) on the same basis as other corporations paying income taxes. Its income will thus not be subject to double taxation. The fact that up until 1946 the appellant was not subject to the same treatment under the Special War Revenue Act as other corporations which paid taxes under the Canadian Income War Tax Act strongly indicates that in 1942 and 1943, when appellant *was not* subject to the general income tax law of Canada, the Special War Revenue Tax, with respect to its application to the appellant, was a tax "in lieu of" an income tax.

(3) *Prior to the enactment of subsection (h) it had been held that the Canadian premium tax was not an income tax within the meaning of Section 131(a)(1) of the revenue acts of 1932 and 1934 (similar to Section 131(a)(1) I.R.C.), but was in the nature of an excise tax.* This reason assigned by the Tax Court for its decision was based entirely upon the cases of *St. Paul Fire & Marine Insurance Co. v. Reynolds*, *Continental Insurance Company v. Commissioner*, and *Helvering v. Queen Insurance Company*, all of which have been discussed at length herein. As previously

pointed out, the expressed intent of Congress in adding subsection (h) to Section 131 I.R.C. was to repudiate the basis of decisions of the courts in those cases. In the Canadian Special War Revenue Tax Law there is no provision in any section that states that it is imposed upon insurance companies for the privilege of exercising their franchise in the Dominion of Canada. There is no section in that law that provides for the revocation of a company's franchise for a failure to pay the tax (See Appendix No. XXVI).

Unless appellant is allowed the foreign tax credit claimed appellant's Canadian income in the amounts of \$509,072.00 and \$540,084.67 for 1942 and 1943 respectively, will be subject to double taxation and the worthwhile purpose of Congress in enacting Section 131 will be defeated. Unless appellant is allowed the foreign tax credit claimed the attempt by Congress to amend and liberalize that section to enable it thereby to carry out its purpose more effectively will be completely thwarted. The applicable case law, for the reasons set forth herein, indicates that to implement and give effect to the purpose of Congress appellant must be allowed the foreign tax credits claimed.



## Section G

### ARGUMENT

#### Limitation Feature

**Section 131(b) of the Internal Revenue Code Requires the Use of Appellant's "Normal-Tax Net Income" (Investment Income) as the Basis for Computing the Limitation on Appellant's Foreign Tax Credit.**

#### I.

*The Internal Revenue Code provides that "normal-tax net income" is the basis for the computation of the limitation on foreign tax credit in the case of a corporation.*

The applicable section of the Internal Revenue Code is Section 131 (a) (b). It was amended by Sections 158(a) and 158(b), of the 1942 Revenue Act. As amended, Section 131(b) provides as follows:

"(b) LIMIT OF CREDIT. The amount of the credit taken under this section shall be subject to each of the following limitations:

"(1) The amount of the credit in respect of the tax paid or accrued to any country shall not exceed the same proportion of the tax against which such credit is taken which the taxpayer's net income from sources within such country bears to his entire net income in the case of a taxpayer other than a corporation or to the sum of the *normal-tax net income* and the amount of the credit for adjusted excess profits net income provided in Section 26(e) in the case of a corporation for the same taxable year; and

"(2) The total amount of the credit shall not exceed the same proportion of the tax against which such credit is taken which the taxpayer's net income from sources without the United

States bears to his entire net income, in the case of a taxpayer other than a corporation, or to the sum of the *normal-tax net income* and the amount of the credit for adjusted excess profits net income provided in Section 26(e) in the case of a corporation for the same taxable year.” (Italics ours)

Prior to the 1942 amendment subparagraphs (1) and (2) of Section 131(b) read as follows:

“(1) The amount of the credit in respect of the tax paid or accrued to any foreign country shall not exceed \* \* \* in the case of a corporation the same proportion of the tax against which such credit is taken which the taxpayer’s *normal-tax net income* from sources within such country bears to its entire normal tax net income for the same taxable year; and

“(2) The total amount of the credit shall not exceed, \* \* \* the same proportion of the tax against which such credit is taken which the taxpayer’s *normal-tax net income* from sources without the United States bears to its entire normal-tax net income for the same taxable year; \* \* \*.” (Italics ours)

By its express provisions the calculation of the limitation on foreign tax credit must be based on the “normal-tax net income” of the taxpayer. The language of the section, both prior to the 1942 amendment and as amended in 1942, is very clear and unambiguous on this point. For that reason there is no reason to judicially construe it.

## II.

***The Commissioner's regulations provide that "normal-tax net income" is the basis for the computation of the limitation on foreign tax credits in the case of a corporation.***

Following the 1942 amendment to Section 131(b) the Commissioner issued Regulation 103, Section 19.131.8 , giving his department's interpretation of the statute as amended. According to the Commissioner's regulation the amount of the income and excess profits tax paid or accrued during the taxable year to each foreign country is limited under Section 131(b) by each of the following in the case of a corporation (see Appendix IX) :

- (1) The credit for taxes paid to any one country shall not exceed the proportion of the U. S. income tax against which the credit is taken which the corporation's *normal-tax net income* from sources within the foreign country bears to its entire *normal-tax net income* for the same taxable year;
- (2) And the aggregate credit shall not exceed the proportion of the U. S. income tax which the *normal-tax net income* from all sources without the U. S. bears to the entire *normal-tax net income* for the same taxable year. (Italics ours)

For the purpose of computing the credit in the case of a corporation for a taxable year beginning after December 31, 1941, normal-tax net income from the foreign country or from outside the U. S. means net income from such sources minus the same proportion of the credit under Code Section 26(e) (for adjusted excess profits net income) which the taxpayer's excess

profits net income from such sources bears to its entire excess profits net income for the same taxable year. While the excess profits feature of the regulation is of interest it is only indirectly pertinent because appellant did not pay any excess profits tax either within or outside of the United States for the taxable years 1942 and 1943.

Since each of these limitations is applicable the calculation under each gives in effect a tentative credit; the allowable credit is that amount which produces the smaller credit. That amount may be applied as a credit against the taxpayers' U. S. income for income or excess profits taxes paid or accrued to a foreign country.

This regulation is very largely a paraphrasing of the wording of the statute itself. It indicates that in the case of a corporation for the taxable years beginning after December 31, 1939, and prior to January 1, 1942, "*the normal-tax net income*" is the basis for the credit, and that for taxable years beginning after December 31, 1941, the "*normal-tax net income*" and the amount of credit for "*adjusted excess profits net income*" forms the basis for the credit. Since the appellant during the tax years 1942 and 1943, did not pay an excess profits tax under Section 26(e) and therefore is not entitled to any credit for adjusted excess profits tax, in accordance with 26(e), appellant's "*normal-tax net income*" formed the sole basis for the computation of the limitation on its foreign tax credit according to the terms of the Commissioner's regulation.



## III.

*Appellant's "normal-tax net income" as shown on its income tax return form 1120 M is its only statutory "normal-tax net income" and therefore must be the basis for the computation of the limitation on its foreign tax credit.*

As previously mentioned in a preceding part, prior to 1942 mutual fire insurance companies such as the appellant were either exempt from income tax under Section 101(11) (Appendix No. XVII) and corresponding provisions of earlier revenue acts, or no income tax was ordinarily paid by them under Section 207 (see Report of Committee on Ways and Means, Cumulative Bulletin 1942-3, Sec. 147 pp. 395 and 456 Appendix No. VIII).

The Revenue Act of 1942, also discussed in a preceding part, amended Section 101(11) to limit the exemption of mutual fire insurance companies, such as appellant to those companies with an annual gross income of \$75,000 or less, thus causing all of the larger mutual fire insurance companies to become taxable under Section 207 (Appendices Nos. VIII and XVIII).

The Revenue Act of 1942 also amended Section 207 by repealing the former provision under which mutual fire insurance companies such as the appellant ordinarily paid no income tax. As previously pointed out in another part, in its place there was enacted an entirely new tax plan for such mutual insurance companies. That plan is unique in Federal Income Tax Law. Under Section 207 as amended, mutual fire insurance companies are taxed:

- (1) On net investment income at corporation tax rates; or
- (2) On gross amount of income at the rate of 1%. taxes being payable on whichever of the two plans produces the greater tax.

A mutual insurance company taxable under Section 207 must make both tax calculations indicated above as (1) and (2) for each tax year on form 1120M. Then it pays whichever of the two taxes is the greater.

The Commissioner has developed a special income tax return for mutual fire insurance companies taxable under Section 207. It is Form 1120M. On this return a mutual company develops its net income from interest, dividends, rent and capital gains. From such net income it develops its normal-tax net income and its surtax net income. To these it applies the normal and surtax rates applicable to corporations generally. The tax on net investment income is thus computed.

Form 1120M also provides for the computation of the tax on "gross amount of income" at 1%. "Gross amount of income," as previously indicated, is composed of net premiums and gross investment income.

Having made both of the two separate calculations on Form 1120M the mutual company takes the greater figure as its federal income tax before the application of any foreign tax credit. If a foreign tax credit is available to the mutual insurance company this is the final calculation on Form 1120M.

The examination of any mutual insurance company's income tax return for a single year will reveal whether the amount of its Federal income tax for that

year is the result of the investment income basis of computation, or the gross amount of income 1% computation, but the final figure, whichever it may be, is that mutual company's Federal income tax.

Thus one of the prerequisites for the determination of appellant's tax under Section 207 I.R.C. is for it to determine and report its "normal-tax net income" as required by Section 207(a) (1) (A) (Appendix No. II).

This normal-tax net income is always computed on the basis of the investment income. For mutual insurance companies other than life or marine Section 207 (b) I.R.C. (Appendix No. III) gives the statutory definition of income of such companies. It defines gross investment and net income of mutual insurance companies, other than life or marine, such as appellant. From that definition it is necessary to turn to Section 13(a) (Appendix No. IV) to arrive at the statutory definition of "normal-tax net income."

Where a mutual fire insurance company, such as appellant, pays its Federal income tax under the provisions of Section 207, on the basis of its net investment income at corporate rates (because that basis had produced the higher tax) the normal-tax net income serves directly to produce the figure for which income tax is payable. According to the position taken by the Commissioner he would not, under such circumstances, question the use of appellant's normal-tax net income for purposes of computing the limitation on its foreign tax credit.

The Commissioner argues that when the circumstances are such that a corporation actually pays Fed-

eral income tax under the provisions of Section 207 on the basis of its "gross amount of income" as defined in Section 207 I.R.C. the "*gross amount of income*" should be used in the place of its *normal-tax net income* in computing the limitation upon its foreign tax credit. That is not a proper or a permissible interpretation of the provisions of the Internal Revenue Code as the law was passed by Congress.

#### IV.

***The only permissible construction of Section 131 (b) indicates that appellant is entitled to the foreign tax credit claimed.***

It is, in effect, the contention of the Commissioner that the words "*gross amount of income*" should be substituted for the words "*normal-tax net income*" where, as in the instant case, the tax which is actually paid is based upon the appellant's "gross amount of income." The law does not permit such a strained construction of the statute, nor will it permit an alteration of the plain language of the statute to conform to the contention of the Commissioner. Actually the wording of Section 131 (b) is so clear that there is no need to construe it. It is only necessary to apply it. In applying it to the facts of this case it is advisable to consider that:

(1) The purpose and intention of Congress and the object of the enactment of the particular section must be considered. *Blake v. National City Bank of New York* (1875) 90 U.S. 119, 23 L. ed. 307, 2 A.F.T.R. 2339; *Burnet v. Chicago Portrait Co.* (1932) 285 U.S. 1, 76 L.ed. 587, 10 A.F.T.R. 800.



(2) The statute must be construed so as not to extend its provisions by implication beyond the clear import of the language used and in cases of doubt they are to be construed most broadly against the government and in favor of the citizen. *Gould v. Gould* (1917) 245 U.S. 151, 152, 62 L. ed. 211, 213, 3 A.F.T.R. 2958.

(3) Where the meaning of particular words are in doubt the literal or popular meaning of the words must be employed. *U.S. v Merriam* (1923) 263 U.S. 179, 187, 68 L.ed. 240, 244, 29 A.L.R. 1547, 44 Sup. Ct. 694, 4 A.F.T.R. 3673; *Crooks v. Harrelson* (1930) 282 U.S. 55, 75 L.ed. 156, 9 A.F.T.R. 571; *Deputy v. DuPont* (1940) 308 U.S. 488, 84 L.ed. 417, 23 A.F.T.R. 808.

There is only one construction of Section 131(b) that is permissible. The section must be construed to mean what it says in language that is clear and unambiguous, namely, that in the case of a corporation the limitation upon its foreign tax credit must be calculated on the basis of its normal-tax net income.

When a mutual fire insurance company, such as appellant, pays its federal income tax on the basis of net premiums plus gross investment income (gross amount of income) at the rate of 1% (where that basis produces the greater tax) its normal-tax net income does not directly produce the figure upon which the income tax is actually paid. That, however, does not form a logical basis for construing the phrase "normal-tax net income" to mean net premiums plus gross investment income when such is the actual basis of the tax paid. If Congress had so intended Congress could have so provided in language that was more clearly an expression of such intention.

The fact that Congress had no such intention is established by the report of the Committee on Finance of the Senate which indicates that the Committee gave careful consideration to the amendment of subsection (b) of Section 131 and intended the "normal-tax net income" to be the basis for the computation of the limitation factor for foreign tax credits in the case of all corporations (see Appendix XIII). If the terms of the statute are not extended by implication, indeed if the words employed are to be given their ordinary literal meaning the limitation upon appellant's foreign tax credit must be computed upon the basis of its "normal-tax net income" as developed in its returns for the years 1942 and 1943.

In this case if the limitation upon appellant's foreign tax credit is calculated on the basis of its "normal-tax net income" as produced on its returns for the years 1942 and 1943, then appellant is entitled to the full amount of the tax credit claimed (see Appendices Nos. XI and XII).

For the reasons set forth herein appellant is entitled to the full amount of the foreign tax credit claimed.

## CONCLUSION

For all the reasons set forth in the preceding parts of appellant's brief it is respectfully submitted that it has been established that the Tax Court's interpretation of Section 131(h) I.R.C. was erroneous. Since the Tax Court did not express its opinion regarding the application of Section 131(b) I.R.C. it is respectfully requested that the decision of the Tax Court be reversed, and that this court determine that under Section 131 I.R.C. appellant is entitled to the full amount of the foreign tax credit claimed.

It is therefore respectfully requested that this court enter judgment in favor of the appellant, setting aside the deficiencies in appellant's income taxes in 1942 and 1943 in the respective amounts of \$5,089.03 and \$5,347.81, and allowing appellant income tax refunds for those years in the amounts of \$10,183.13 and \$10,854.73, respectively.

Respectfully submitted,

JO DUDLEY COOK,  
FREDERICK J. ORTH,

*Of Counsel:*

*Attorneys for Appellant.*

RODE, COOK & WATKINS,  
217 Pine Street,  
Seattle 1, Washington.





## APPENDICES

### Preface

These appendices are furnished with Appellant's brief to facilitate this Court's reference to the pertinent regulations, statutes and reports referred to in Appellant's brief.

Appendices Nos. I - VI inclusive, and XV - XVIII inclusive, contain the pertinent provisions of the credit and limitation features of the Internal Revenue Code, the provisions of the section under which Appellant was taxed, and all other sections to which reference is necessary in determining Appellant's foreign tax credits.

Appendices Nos. VII - X inclusive, and XIII and XIV set forth the pertinent regulations in toto, with quotations at length from appropriate Cumulative Bulletins.

For the convenience of the Court, Appendices Nos. XI and XII summarize in tabular form what Appellant contends is the correct manner of calculating the amount of Appellant's foreign tax credit for 1942 and 1943.

The history of the taxation of insurance companies, stock and mutual, in Canada and the United States is concisely summarized in tabular form in Appendix No. XIX.

Appendices Nos. XX - XVII inclusive, summarize as concisely as possible all pertinent rulings of the Commissioner of Internal Revenue.

In Appendices Nos. XXIII and XXIV the pertinent case law is succinctly digested.

Wherever excerpts are quoted in the brief an effort has been made to set forth at length in these appendices the entire quotation from which they were taken. Appendix No. XXV contains pertinent quotations from the Canadian Parliamentary debates.

Appendix No. XXVI contains the penalty provision of the Canadian Special War Revenue Act.

**APPENDIX No. 1**

**“SUPPLEMENT C - - - CREDITS AGAINST TAX  
TAXES OF FOREIGN COUNTRIES AND POSSESSIONS  
OF UNITED STATES**

**“Sec. 131(a)**

“(a) ALLOWANCE OF CREDIT.—If the taxpayer chooses to have the benefits of this section, the tax imposed by this chapter, except the tax imposed under section 102 or section 450, shall be credited with:

“(1) CITIZENS AND DOMESTIC CORPORATIONS.—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States; and \* \* \*

“Such choice may be made or changed at any time prior to the expiration of the period prescribed for making a claim for credit or refund of the tax imposed by this chapter.”

**“Sec. 131(b)**

“(b) LIMIT ON CREDIT.—The amount of the credit taken under this section shall be subject to each of the following limitations:

“(1) The amount of the credit in respect of the tax paid or accrued to any country shall not exceed, in the case of a taxpayer other than a corporation, the same proportion of the tax against which such credit is taken, which the taxpayer's net income from sources within such country bears to his entire net income for the same taxable year, or in the case of a corporation, the same proportion of the tax against which such credit is taken, which the taxpayer's normal-tax net income from sources within such country bears to its entire normal-tax net income for the same taxable year; and

“(2) The total amount of the credit shall not exceed, in the case of a taxpayer other than a corporation, the same proportion of the tax against which such credit is taken, which the taxpayer’s normal-tax net income from sources without the United States bears to its entire normal-tax net income for the same taxable year; and

“Sec. 131(h)

“(h) CREDIT FOR TAXES IN LIEU OF INCOME, ETC., TAXES.—For the purposes of this section and section 23(c)(1), the term ‘income, war-profits, and excess-profits taxes’ shall include a tax paid in lieu of a tax upon income, war-profits, or excess-profits otherwise generally imposed by any foreign country or by any possession of the United States.”

## APPENDIX No. II

### “MUTUAL INSURANCE COMPANIES OTHER THAN LIFE OR MARINE

“Sec. 207(a)

“(a) IMPOSITION OF TAX.—There shall be levied, collected, and paid for each taxable year upon the income of every mutual insurance company (other than a life or a marine insurance company or a fire insurance company subject to the tax imposed by section 204 and other than an interinsurer or reciprocal underwriter) a tax computed under paragraph (1) or paragraph (2) whichever is the greater and upon the income of every mutual insurance company (other than a life or marine insurance company or a fire insurance company subject to the tax imposed by section 204) which is an interinsurer or reciprocal underwriter, a tax computed under paragraph (3):

“(1) If the corporation surtax net income is over \$3,000 a tax computed as follows:

“(A) Normal Tax.—A normal tax on the normal-tax net income, computed at the rates provided in section 13 or section 14(b), or 30 per centum of the amount by which the normal-tax net income exceeds \$3,000, whichever is the lesser; plus

“(B) Surtax.—A surtax on the corporation surtax net income, computed at the rates provided in section 15(b), or 20 per centum of the amount by which the corporation surtax net income exceeds \$3,000, whichever is the lesser.

“(2) If for the taxable year the gross amount of income from interest, dividends, rents and net premiums, minus dividends to policyholders, minus the interest which under section 22(b)(4) is excluded from gross income, exceeds \$75,000, a tax equal to the excess of —

“(A) 1 per centum of the amounts so computed, or 2 per centum of the excess of the amount so computed over \$75,000, whichever is the lesser, over

“(B) the amount of the tax imposed under Subchapter E of Chapter 2.”

### **APPENDIX No. III**

#### **“MUTUAL INSURANCE COMPANIES OTHER THAN LIFE OR MARINE**

“Sec. 207(b)

“(b) DEFINITION OF INCOME, ETC.—In the case of an insurance company subject to the tax imposed by this section —

“(1) GROSS INVESTMENT INCOME. — ‘Gross investment income’ means the gross amount of income during the taxable year from interest, dividends, rents, and gains from sales or exchanges of capital assets to the extent provided in section 117;

“(2) NET PREMIUMS. — ‘Net premiums’ means gross premiums (including deposits and assessments) written or received of insurance contracts during the taxable year less return premiums and premiums paid



or incurred for reinsurance. Amounts returned where the amount is not fixed in the insurance contract but depends upon the experience of the company or the discretion of the management shall not be included in return premiums but shall be treated as dividends to policyholders under paragraph (3);

“(3) **DIVIDENDS TO POLICYHOLDERS.**—‘Dividends to policyholders’ means dividends and similar distributions paid or declared to policyholders. The term ‘paid or declared’ shall be construed according to the method regularly employed in keeping the books of the insurance company;

“(4) **NET INCOME.**—The term net income means the gross investment income less —

“(A) Tax-free Interest. \* \* \*

“(B) Investment Expenses. \* \* \*

“(C) Real Estate Expenses. \* \* \*

“(D) Depreciation. \* \* \*

“(E) Interest Paid or Accrued. \* \* \*

“(F) Capital Losses. \* \* \*”

## **APPENDIX No. IV**

### **“TAX ON CORPORATIONS IN GENERAL**

#### **“Sec. 13(a)**

“(a) **DEFINITIONS.** — For the purpose of this chapter —

“(1) **ADJUSTED NET INCOME.**—The term ‘adjusted net income’ means the net income minus the credit provided in section 26(a), relating to interest on certain obligations of the United States and Government corporations.

“(2) **NORMAL-TAX NET INCOME.**—The term ‘normal-tax net income’ means the adjusted net income minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26(e) and minus the credit for dividends received provided in section 26(b).”

“Sec. 13(b)

“(b) IMPOSITION OF TAX.—There shall be levied, collected, and paid for each taxable year upon the normal-tax net income of every corporation the normal-tax net income of which is more than \$25,000 (except a corporation subject to the tax imposed by section 14, section 231(a), Supplement G, or Supplement Q) whichever of the following taxes is the lesser:

“(1) GENERAL RULE.— A tax of 24 per centum of the normal-tax net income; or

“(2) ALTERNATE TAX (CORPORATIONS WITH NORMAL-TAX NET INCOME OVER \$25,000 BUT NOT OVER \$50,000).—A tax of \$4,250, plus 31 per centum of the amount of the normal-tax net income in excess of \$25,000.”

**APPENDIX No. V**

**“SURTAX ON CORPORATIONS**

“Sec. 15(a)

“(a) CORPORATION SURTAX NET INCOME.—For the purposes of this chapter, the term ‘corporation surtax net income’ means the net income minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26(e) and minus the credit for dividends received provided in section 26(b) (computed by limiting such credit to 85 per centum of the net income reduced by the credit for income subject to the tax imposed by Subchapter E of Chapter 2 in lieu of 85 per centum of the adjusted net income so reduced), and minus, in the case of a public utility, the credit for dividends paid on its preferred stock provided in section 26(h). For the purposes of this subsection dividends received on the preferred stock of a public utility shall be disregarded in computing the credit for dividends received provided in section 26(b).

“Sec. 15(b)

“(b) IMPOSITION OF TAX.—There shall be levied, collected, and paid for each taxable year upon the corporation surtax net income of every corporation (except a Western Hemisphere Trade Corporation as defined in section 109, and except a corporation subject to the tax imposed by section 231(a), Supplement G, or Supplement Q), a surtax as follows:

“1. Surtax net income not over \$25,000. \* \* \*

“2. Surtax net incomes over \$25,000 but not over \$50,000. \* \* \*

“3. Surtax net incomes over \$50,000.—Upon corporation surtax net incomes over \$50,000, 16 per centum of the corporation surtax net income.”

**APPENDIX No. VI**

**“CREDITS OF CORPORATIONS**

“Sec. 26(a)

“(a) INTEREST ON OBLIGATIONS OF THE UNITED STATES AND ITS INSTRUMENTALITIES.—The amount received as interest upon obligations of the United States or of corporations organized under Act of Congress which is allowed to an individual as a credit for purposes of normal-tax by section 25(a)(1) or (2). (For reduction of credit under this subsection on account of amortizable bond premium, see section 125).

“Sec. 26(b)

“(b) DIVIDENDS RECEIVED.—85 per centum of the amount received as dividends from a domestic corporation which is subject to taxation under this chapter, but not in excess of 85 per centum of the adjusted net income reduced by the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in subsection (e).

The credit allowed by this subsection shall not be allowed in respect of dividends received from a corporation organized under the China Trade Act, 1922, 42 Stat. 849 (U.S.C., Title 15, C. 4), or from a corporation which under section 251 is taxable only on its gross income from sources within the United States by reason of its receiving a large percentage of its gross income from sources within a possession of the United States."

"Sec. 26(e)

"(e) INCOME SUBJECT TO EXCESS-PROFITS TAX.—In the case of any corporation subject to the tax imposed by Subchapter E of Chapter 2, an amount equal to its adjusted excess-profits net income (as defined in section 710(b). \* \* \*"

Subchapter E of Chapter 2 \* \* \* Excess Profits Tax.

**APPENDIX No. VII**

**"III.—TAXATION OF CERTAIN TYPES OF CORPORATIONS**

**"2. MUTUAL INSURANCE COMPANIES OTHER THAN LIFE. —**

"The revenue derived from mutual insurance companies is negligible. The reason lies in the broad language of the exception provision and in the ineffective language of the taxing provisions. Section 144 of the bill makes the exemption provision explicit, limiting it to companies of designated size. It also completely revises the taxing provisions, basing the levy on underwriting and investment income, in a manner similar to that applied to stock insurance companies other than life. At the same time due regard is given the mutual character of these companies through the reduction of underwriting income by dividends to policyholders out of premiums and surplus apportioned to them,



and by additions to surplus apportioned to policyholders.”  
Cumulative Bulletin 1942-2, p. 395.

### APPENDIX No. VIII

Cumulative Bulletin 1942-2, p. 456.

#### “Section 147.—MUTUAL INSURANCE COMPANIES OTHER THAN LIFE. —

“Most mutual insurance companies other than life, large as well as small, are given an outright exemption from taxation under section 101(11), although that section was originally designed to exempt only small and local mutual companies. The remaining mutual companies, with a few exceptions, ordinarily pay no tax under the present method of computing their income even though not specifically exempted from the tax.

“The exemption provided in section 101(11) has been revised so that it will be limited to mutual companies or associations (including interinsurers and reciprocal underwriters) writing insurance contracts solely on a mutual basis, if the mean of the ledger assets held at the beginning and end of the taxable year does not exceed \$100,000. Practically all of the farmers’ and other small and local mutual companies have ledger assets of less than \$100,000 and accordingly will not be required to file income tax returns or pay any income taxes. It is estimated that over 80 per cent of all companies will be exempt from filing returns under this provision. In addition, even where ledger assets exceed \$100,000, and an income tax return must be filed, it is provided under section 207(a) that no income tax is payable unless the corporation surtax net income (which may be greater than, but can never be less than, the normal tax net income) is over \$50,000. Only the larger companies will pay a tax under these provisions. Accord-

ingly, these provisions will impose no hardship upon farmers' or other small and local mutual insurance companies other than life.

"In case of mutual insurance companies other than life which are not granted exemption under section 101(11), it is proposed to subject such companies to income tax on the sum of their investment and underwriting income in a manner somewhat similar to that used under section 204 (relating to insurance companies other than life or mutual). \* \* \*"

## APPENDIX No. IX

### "Reg. 103, Sec. 19.131-8. LIMITATIONS ON CREDIT FOR FOREIGN TAXES.

"The amount of the income and profits taxes paid or accrued (including the taxes which, in accordance with the provisions of section 131(f), are deemed to have been paid) during the taxable year to each foreign country or possession of the United States, limited under section 131(b)(1) so as not to exceed that proportion of the tax against which credit is taken which the taxpayer's net income from sources within such country or possession bears to (a) his entire income from sources within such country or possession bears to (a) his entire net income, or (b) for taxable years beginning after December 31, 1939, and prior to January 1, 1942, the normal-tax net income in the case of a corporation, or (c) (for taxable years beginning after December 31, 1941) the sum of the normal-tax net income and the amount of the credit for adjusted excess profits net income provided in section 26(e) in the case of a corporation, for the same taxable year, is the tentative credit in respect of the taxes paid or accrued to such country or possession. The sum of these tentative credits, limited under section 131(b)(2) so as not to

exceed the same proportion of the tax against which credit is taken which the taxpayer's net income from sources without the United States bears to (a) his entire net income, or (b) (for taxable years beginning after December 31, 1939, and prior to January 1, 1942) the normal-tax net income in the case of a corporation, or (c) (for taxable years beginning after December 31, 1941) the normal-tax net income computed without the credit for adjusted excess profits net income provided in section 26(e) in the case of a corporation, for the same taxable year, is the amount allowable as a credit against the income tax under chapter 1 for income or profits taxes paid or accrued to foreign countries or possessions of the United States. In computing the tax against which the credit is taken there must, for years beginning after December 31, 1939, and before January 1, 1943, be excluded the tax, if any, imposed by section 102, and for years beginning after December 31, 1942, there must be excluded both the tax imposed by section 102 and the tax imposed by section 450."

## APPENDIX No. X

"Reg. 103, Sec. 19.131-2. MEANING OF TERMS.—The term 'amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year' means taxes proper (no credit being given for amounts representing interest or penalties) paid or accrued during the taxable year on behalf of the taxpayer claiming credit. For the purposes of section 131 and section 23(c)(1) the term 'income, war-profits and excess-profits taxes' includes, for taxable years beginning after December 31, 1941, a tax imposed by statute or decree by a foreign country or by a possession of the United States if (a) such country or possession has in force a general income tax law, (b) the taxpayer claiming the credit would, in the absence of

a specific provision applicable to such taxpayer, be subject to such general income tax, and (c) such general income tax is not imposed upon the taxpayer thus subject to such substituted tax. For example, the A Corporation does business in the X Country which imposes an income tax upon substantially a net income base. The ascertainment of net income, though not the determination of gross income, from sources in X Country is found administratively difficult. The X Country, by decree, provides that corporations circumstanced as was the A Corporation would, in lieu of the income tax at the rate of 20 per cent otherwise payable, be subject to tax at the rate of 10 per cent upon the amount of gross income from X Country. In accordance with such decree, the A Corporation paid X Country the sum of \$25,000 in 1943 with respect to its tax liability to the X Country for the year 1942. Such amount, subject to the applicable limitations, is available as a credit to the A Corporation as foreign income, war-profits or excess-profits taxes against the United States tax liability for the year 1942. 'Foreign country' means any foreign state or political subdivision thereof, or any foreign political entity, which levies and collects income, war-profits, or excess-profits taxes. 'Any possession of the United States' includes, among others, Puerto Rico, the Philippines, and the Virgin Islands. But see (Code) section 251. As to the meaning of 'sources,' see (Code) section 119. (See also (Code) section 3797). (Reg. 103, Sec. 19.131-2.)"



## APPENDIX No. XI

## INCOME TAXES PAYABLE

*Computation of Gross Amount of Income:*

	<i>Taxable Year Ended Dec. 31,</i>	
	1942	1943
Gross (investment income under section 207(a)(1) and (3), page 1 of returns as adjusted by field audit.....	\$ 244,213.81	\$ 267,519.39
Net premiums: United States.....	7,381,054.65	7,758,443.62
Canada, 1942—\$681,111.30 converted at 90.909 $\frac{9}{10}$ %.....	619,191.47	.....
1943—\$684,416.33 converted at 90.909 $\frac{9}{10}$ %.....	.....	622,196.04
Total gross amount of income.....	\$8,244,459.93	\$8,648,159.05
Less: Dividends to Policyholders.....		
United States.....	\$1,347,259.56	\$1,448,978.24
Canada, 1942—\$155,242.77 converted at 90.909 $\frac{9}{10}$ %.....	141,129.65	.....
1943—\$128,382.58 converted at 90.909 $\frac{9}{10}$ %.....	.....	116,711.32
Total dividends.....	\$1,488,389.21	\$1,565,689.56
Interest wholly exempt from tax.....	39,750.00	37,401.52
Total deductions from gross amount of income.....	\$1,528,139.21	\$1,603,091.08
Gross amount of income under Section 207(a)(2).....	\$6,716,320.72	\$7,045,067.97

*Computation of Tax:*

<b>Under Section 207(a)(1) and (3):</b>		
Normal-tax net income, item 19, page 1 of returns as accepted on field audit.....	\$ 126,451.85	\$ 151,828.23
Net income, item 14, page 1 of returns.....	199,657.79	224,927.98
Less: Dividends received credit.....	41,611.33	43,899.32
Surtax net income.....	\$ 158,046.46	\$ 181,028.66
Normal tax at 24% of normal-tax net income.....	30,348.44	36,438.78
Surtax at 16% of surtax net income.....	25,289.43	28,964.59
Total tax under Section 207(a)(1) and (3).....	\$ 55,635.87	\$ 65,403.37
<b>Under Section 207(a)(2):</b>		
Gross amount of income computed above.....	\$6,716,320.72	\$7,045,067.97
Tax at 1%—being the tax payable as it is greater than that computed under 207(a)(1) and (3).....	\$ 67,163.21	\$ 70,450.68
Less: Credit claimed for taxes paid in lieu of income taxes to Canada as provided in Section 131(h), See Appendix No. XII.....	15,272.16	16,202.54
Balance of tax.....	\$ 51,891.05	\$ 54,248.14

# **APPENDIX No. XII** **CREDITS CLAIMED AGAINST INCOME TAXES**

(Developed as provided on Form 1118)

		<i>Taxable Year Ended Dec. 31</i>	
		1942	1943
I.	Normal-tax net income from all sources, item 19, page 1 of returns as accepted on field audit. . . . .	\$126,451.85	\$151,828.23
II.	Total United States income tax as adjusted by field audit. See Appendix No. XI . . . . .	\$ 67,163.21	\$ 70,450.68
1.	Normal-tax net income from sources in Canada (ex. div.)		
	1942—\$41,522.85 converted at 90.909% <sub>C</sub> . . . . .	\$ 37,748.01	
	1943—\$44,885.75 converted at 90.909% <sub>C</sub> . . . . .		\$ 40,805.19
2.	Dividends received from sources in Canada		
	1942—\$105.00 converted at 90.909% <sub>C</sub> . . . . .	95.45	
	1943—\$151.66 converted at 90.909% <sub>C</sub> . . . . .		137.87
3.	Total normal tax net income from sources in Canada. . . . .	\$ 37,843.46	\$ 40,943.06
4. & 7.	Total of taxes paid in Canada (in lieu of income taxes)		
	1942—\$16,799.39 converted at 90.909% <sub>C</sub> . . . . .	\$ 15,272.16	
	1943—\$17,822.81 converted at 90.909% <sub>C</sub> . . . . .		\$ 16,202.54
8.	Ratio of normal-tax net income from sources in Canada to normal-tax net income from all sources (Item 3 divided by Item I) . . . . .	29.927%	26.967%
9.	Amount of tax which may be claimed as credit under limitation of Section 131(b)(1) (Item II, multiplied by Item 8, unless Item 7 is less than such amount, in which case Item 7 must be used) . . . . .	\$ 15,272.16	\$ 16,202.54

**APPENDIX No. XIII**

Internal Revenue Bulletin, Cumulative Bulletin 1942-2

“Section 160. FOREIGN TAX CREDIT. (Page 603).

“\* \* \*

“An amendment to subsection (b) of section 131 was found by your committee to be necessary because of the method for computing ‘normal-tax net income’ provided in section 105 of the bill, amending section 131(a)(2) of the Code. Under existing law in computing ‘normal tax net income’ the excess profits tax imposed under Chapter 2E is allowed as a deduction. Under the revenue bill of 1942, however, the adjusted excess profits net income is deducted from adjusted net income in the ascertainment of ‘normal tax net income.’ To preserve the appropriate ratio between the numerator and the denominator of the limitation fraction under section 131(b), it is necessary that adjusted net income be not reduced by the amount of the adjusted excess profits net income for the purpose of that section, and section 160(d) amends section 131(b) so as to accomplish such result.

“Your committee has given careful consideration to a suggested amendment to section 131 which would in substance provide that the credit for foreign taxes on foreign income not reported in the taxable year because of its being blocked should be deferred and allowed in the taxable year in which such income is released and realized for income tax purposes. The committee has not adopted such an amendment for the reason that it believes the amendment to be unnecessary. Under a proper interpretation of existing law, the credit for foreign taxes, as well as the various allowable deductions, follows the income into the taxable year in which it is realized for purposes of the income tax law. The committee feels, in view of the importance of this

question to a large number of taxpayers, that the matter is one which it would be appropriate to cover specifically by departmental regulation.”

Senate Finance Committee, Senate Report No. 1631, Seventy-seventh Congress, Second Session Calendar No. 1683 (October 2, 1942).

#### **APPENDIX No. XIV**

“Internal Revenue Bulletin, Cumulative Bulletin 1942-2, Sec. IV. TAXATION OF CERTAIN TYPES OF CORPORATION. §1. Mutual Insurance Companies Other Than Life or Marine. Page 531.

“Under the House bill, mutual insurance companies other than life were to be taxed on the basis of their underwriting and investment income. The objective was a taxing system substantially the same as that which has been applied to stock insurance companies other than life since 1921. In recognition of the quality of mutuality, however, two special deductions were allowed. One of these was dividends to policyholders; the other, surplus apportioned to policyholders. The latter was found to involve concepts generally novel to the business of writing insurance. Dividends to policyholders, moreover, were deductible only to the extent they were paid out of premiums received or surplus apportioned to policyholders; to the extent they were paid out of investment income, they were disallowed. For the purpose of determining their deductibility, dividends were assumed to be paid out of investment income to the extent of such income remaining after the deduction of the tax allowable thereto.

“Your committee carefully considered the house bill plan and various modifications of it in attempting to define and tax underwriting income in an equitable manner. No adequate method to accomplish that result was developed.



“The committee bill, therefore, proposes to tax mutual insurance companies other than life or marine upon that one of the following two bases which produces the greater tax. One of these bases is net investment income, to which are applied the rates applicable to corporate incomes generally. The other base is the gross amount of income from interest, dividends, rents and net premiums, less dividends to policyholders and wholly tax-exempt interest. To this base the rate of 1 per cent is to apply. Mutual marine insurance companies are taxable under the provisions applicable to stock insurance companies other than life. This is essentially the basis upon which they are taxed under existing law. Reciprocal underwriters and interinsurers are subject to the net investment income tax and not to the 1 per cent tax.

“It is believed that the plan of taxation recommended by your committee will operate much more equitably than the House bill plan, or any modification thereof incorporating the principle of taxing underwriting income, and will have no regulatory effect upon the industry. At the same time, it offers no unusual administrative difficulties and will yield a considerable amount of revenue.”

Senate Finance Committee, Senate Report No. 1631, Seventy-seventh Congress, Second Session Calendar No. 1683 (October 2, 1942).

## **APPENDIX No. XV**

### **REVENUE ACT OF 1917**

“Title V.—WAR TAX ON FACILITIES FURNISHED BY PUBLIC UTILITIES AND INSURANCE.

“Sec. 504. That from and after the first day of November, nineteen hundred and seventeen, there shall be levied, assessed, collected, and paid the following taxes on issuance of insurance policies:

“(a) Life insurance: \* \* \*

“(b) Marine, inland, and fire insurance: A tax equivalent to 1 cent on each dollar or fractional part thereof of the premium charged under each policy of insurance or other instrument by whatever name the same is called whereby insurance is made or renewed upon property of any description (including rents or profits), whether against peril by sea or inland waters, or by fire, lightning, or other peril: Provided, That policies of reinsurance shall be exempt from the tax imposed by this subdivision;

“(c) Casualty insurance: \* \* \*.”

## **APPENDIX No. XVI**

### **REVENUE ACT OF 1918**

“Title V. — TAX ON TRANSPORTATION AND OTHER FACILITIES, AND ON INSURANCE.

“Sec. 503. That from and after April 1, 1919, there shall be levied, assessed, collected, and paid, in lieu of the taxes imposed by section 504 of the Revenue Act of 1917, the following taxes on the issuance of insurance policies, including, in the case of policies issued outside of the United States (except those taxable under subdivision 15 of Schedule A of title XI), their delivery within the United States by any agent or broker, whether acting for the insurer or the insured; such taxes to be paid by the insurer, or by such agent or broker:

“(a) Life insurance: \* \* \*.”

“(b) Marine, inland, and fire insurance: A tax equivalent to 1 cent on each dollar or fractional part thereof of the premium charged under each policy of insurance or other instrument by whatever name the same is called whereby insurance is made or renewed upon property of any description (including rents or profits), whether against peril by sea or inland waters, or by fire or lightning, or other peril;

“(c) Casualty insurance: \* \* \*.”

## APPENDIX XVII

(Prior to 1942 amendment)

### “EXEMPTIONS FROM TAX ON CORPORATIONS.

“Sec. 101. The following organizations shall be exempt from taxation under this chapter:

“(11) Farmers’ or other mutual hail, cyclone, casualty, or fire insurance companies or associations (including interinsurers and reciprocal underwriters) the income of which is used or held for the purpose of paying losses or expenses.”

## APPENDIX No. XVIII

(Subsequent to 1942 amendment)

### “EXEMPTIONS FROM TAX ON CORPORATIONS.

“Sec. 101 (Internal Revenue Code). The following organizations shall be exempt from taxation under this chapter: \* \* \*

“(11) Mutual insurance companies or associations other than life or marine (including interinsurers and reciprocal underwriters) if the gross amount received during the taxable year from interest, dividends, rents and premiums (including deposits and assessments) does not exceed \$75,000; \* \* \*”

## APPENDIX No. XIX

	<i>By United States</i>		<i>By Dominion of Canada</i>	
	<i>Mutual</i>	<i>Stock</i>	<i>Mutual</i>	<i>Stock</i>
	<i>Insurance</i>	<i>Insurance</i>	<i>Insurance</i>	<i>Insurance</i>
	<i>Companies</i>	<i>Companies</i>	<i>Companies</i>	<i>Companies</i>
1917-1920:				
Subject to Income Tax....	No	Yes	No	Yes
Subject to Premium Tax...	Yes	Yes	Yes <sup>(1)</sup>	Yes <sup>(1)</sup>
1921-1941:				
Subject to Income Tax....	No	Yes	No	Yes
Subject to Premium Tax...	No	No	Yes <sup>(1)</sup>	Yes <sup>(1)</sup> (2)
1942-1946:				
Subject to Income Tax....	Yes <sup>(3)</sup>	Yes	No	Yes
Subject to Premium Tax...	No	No	Yes <sup>(4)</sup>	Yes <sup>(5)</sup>
1946 to present:				
Subject to Income Tax....	Yes <sup>(3)</sup>	Yes	Yes	Yes
Subject to Premium Tax...	No	No	Yes <sup>(5)</sup>	Yes <sup>(5)</sup>

<sup>1</sup>at rate of 1% (collection suspended from Dec. 31, '28 to Jan. 1 '32).

<sup>2</sup>Deductible from amount of Income Tax otherwise payable.

<sup>3</sup>On one of two bases (1) investment income at corporate rates or (2) net premiums, plus gross investment income at 1%.

<sup>4</sup>At rate of 3% and 4% of net premiums.

<sup>5</sup>At rate of 2%.

## APPENDIX No. XX

Construing the foreign tax credit provisions of the Revenue Acts from 1917 to 1942, the Commissioner ruled that the foreign tax should be allowed as credit in the following:

I. T. 1522, I-2 C.B. 199 (Rev. Acts '18 and '21 )Cuban tax;  
I. T. 2070, III-2 C.B. 250 (Rev. Acts '21 and '24) Bolivian tax Mining Profits;

I. T. 2118, III-2 C.B. 251 (Rev. Acts '21 and '24) Puerto Rican Income tax;

G.C.M. 6042, VIII-1 C.B. 184 (Rev. Act '22) Chilean tax on Profits;



- G.C.M. 800, V-2 C.B. 75 (Rev. Act '22) Brazilian tax on Gross Income;
- G.C.M. 7629, IX-1 C.B. 146 (Rev. Act '28) Cuban "net profit" tax;
- I. T. 2445, VIII-1 C.B. 102 (Rev. Act '28) Ecuador tax;
- I. T. 2762, XIII-1 C.B. 64 (Rev. Act '32) Argentine Dividend tax;
- I. T. 3313, 1939-2 C.B. 171 (Rev. Act '32) Brazilian Profits tax;
- I. T. 2964, XV-1 C.B. 138 (Rev. Act '36) Canada tax on Copy Right use;
- G.C.M. 14625, XIV-1 C.B. 114 (Rev. Act '36) Mexican Absenteeism tax;
- I. T. 3171, 1938-1 C.B. 192 (Rev. Act '36) English Profits tax;
- G.C.M. 21227, 1939-1 C.B. 191 (Rev. Act '36) Canadian Dividend tax; (Part 1)
- I. T. 3371, 1940-1 C.B. 102 (Rev. Act '36) Netherlands Profits tax;
- I. T. 3385, 1940-1 C.B. 103 (Rev. Acts '36 and '38) Mexican Dividend tax;
- I. T. 3464, 1941-1 C.B. 257 (Rev. Act '41) Canadian Net Income tax.

## APPENDIX No. XXI

Construing the foreign tax credit provisions of the Revenue Acts from 1917 to 1942, the Commissioner ruled that the foreign tax should be denied as a credit in the following:

- O. D. 372, 2 C.B. 115 (Rev. Act '17) Cuban tax on Sugar Produced;
- I. T. 2499, VIII-2 C.B. 325 (Rev. Act '18) Peruvian Sugar Export tax;
- I. T. 1444, I-2 C.B. 168 (Rev. Act '21) Latvian tax on Living Expenses;

- G.C.M. 8478, IX-2 C.B. 224 (Rev. Act '26) French Transfer tax;
- I. T. 2596, X-2 C.B. 184 (Rev. Act '28) Cuban tax on Gross Revenues;
- G.C.M. 11039, X-2 C.B. 118 (Rev. Act '28) Film Hire tax;
- I. T. 3040, 1937-1 C.B. 109 (Rev. Act '36) Mexican tax on capital export;
- I. T. 3138, 1937-2 C.B. 230 (Rev. Acts '32 and '34) Canadian Net Premium tax;
- I. T. 3211, 1938-2 C.B. 177 (Rev. Acts '34 and '36) Net Premium tax by Canadian Provinces;
- I. T. 2909, XIV-2 C.B. 136 (Rev. Act '34) Quebec Mining Profits tax;
- I. T. 3429, 1940-2 C.B. 136 (Rev. Act '40) Cuban Gross Receipts;
- I. T. 3433, 1940-2 C.B. 137 (Rev. Act '40) Cuban Mineral Fuel tax.

## APPENDIX No. XXII

Construing Section 131 of the Internal Revenue Code from the enactment of the 1942 amendment to date, the Commissioner ruled that the foreign tax should be allowed in the following:

- I. T. 3565, 1942-2, C.B. 135 (1942) Cuban tax on Salaries and Wages;
- I. T. 3683, 1944, C.B. 290 (1944) Mexican tax on Dividends;
- I. T. 3774, 1945, C.B. 204 (1945) Tax on Net Profits;
- I. T. 3778, 1946-1, C.B. 11 (1946) Tax on Net Profits;
- I. T. 3837, 1947-1, C.B. 56 (1947) Argentine Income and Profit tax;
- I. T. 3903, 1948-8, C.B. 5 (1948) Cuban Gross Revenue tax.

# APPENDIX No. XXIII

Construing the foreign tax credit provisions of U. S. Revenue Acts prior to 1942 the following decisions held that the foreign tax should be allowed as a foreign tax credit:

<i>Herbert Ide Kien v. Commissioner</i> (1929) 15 B.T.A. 1243.....	French income tax
<i>Havana Electric Ry. Light &amp; Power Co. v. Commissioner</i> (1936) 34 B.T.A. 782..	Cuban net profit tax
<i>Seatrains Lines, Inc. v. Commissioner</i> (1942) 46 B.T.A. 1076.....	Gross revenue tax
<i>Santa Eulalia Mining Co. v. Commissioner</i> (1943) 2 T.C. 241.....	Gross revenue tax
<i>Queen Insurance Company of America v. Commissioner</i> (August 18, 1939) 40 B.T.A. 484 <sup>(1)</sup> .....	Canadian income and premium taxes.
<i>Continental Insurance Co. v. Commissioner</i> (Sept. 9, 1939) 40 B.T.A. 540 <sup>(2)</sup> .	Canadian income and premium taxes.

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Overruled by *Helvering v. Queen Ins. Co.* (1940) 115 F.(2d) 341, 25 A.F.T.R. 996.

Part of decision overruled by *Helvering v. Queen Ins. Co.*, *supra*, part of decision affirmed by District Court in *St. Paul Fire & Marine Insurance Co. v. Reynolds* (1942) 44 F. Supp. 863, 29 A.F.T.R. 592.

## APPENDIX No. XXIV

Construing the foreign tax credit provisions of the U. S. Revenue Acts prior to 1942 the following decisions held that the foreign tax *should not be* allowed as a foreign tax credit:

*Eitingon-Schild Co. Inc. and Subsidiaries*

*v. Commissioner* (1931) 21 B.T.A. 1163. French turnover tax.

*Havana Elec. Ry. Light & Power Co. v.*

*Commissioner* (1934) 29 B.T.A. 1151.. Cuban tax on doing business.

*Mallouck et al. v. Commissioner* (1936)

34 B.T.A. 269..... Philippine Island privilege tax.

*New York & Honduras Rosario Mining Co.*

*v. Commissioner* (1947) 8 T.C. 1232<sup>(4)</sup>.. Profits tax on mine exploitation.

*Keasbey and Mattison Co. v. Rothensies*

(1943) 133 F.(2d) 894, 30 A.F.T.R. 990. Profits tax on mining.

*Helvering v. Queen Insurance Co.* (1940)

115 F.(2d) 341, 25 A.F.T.R. 996<sup>(1)</sup>.... Canadian income and premium tax.

*Continental Insurance Co. v. Commissioner*

(Sept 9, 1939) 40 B.T.A. 540<sup>(2)</sup>.... Canadian premium tax.

*St. Paul Fire & Marine Insurance Co. v.*

*Reynolds* (1942) 44 F. Supp. 863<sup>(3)</sup>,

29 A.F.T.R. 592..... Canadian premium tax.

<sup>1</sup>Overruling B.T.A. decision in *Queen Insurance Co. v. Commissioner* (1939) 40 B.T.A. 484.

<sup>2</sup>Partly affirmed in *St. Paul Fire & Marine Insurance Co. v. Reynolds*, *supra*.

<sup>3</sup>District Court affirmed decision of B.T.A. in *Continental Insurance Co. v. Commissioner* (1939) 40 B.T.A. 540.

<sup>4</sup>Tax Court decision overruled by U. S. Court of Appeals in 168 F. (2d) 745, 36 A. F. T. 1115.



## APPENDIX XXV

In the House of Commons Debates on August 2nd, 1946, the Honorable Douglas Abbott (Acting Minister of Finance), in presenting the proposed 1946 amendment to the Special War Revenue Act stated as follows:

“I have a brief explanation to give here, and in a moment I shall ask one of my colleagues to move an amendment. These resolutions are related to resolution fourteen under the Income War Tax Act, under which it is proposed to withdraw the exemption from income tax at present applying to mutual insurance companies other than life insurance companies. The removal of this exemption from income tax is in accordance with the recommendation of the McDougall commission. *In view of the fact that these mutual insurance companies will no longer be completely exempt from tax, a reduction is being proposed in the premium taxes under the Special War Revenue Act applying to these companies.* (Italics ours)

“The amendments to resolutions 4 and 5 which I shall ask one of my colleagues to move are the result of further consideration of premium taxes since the budget was introduced. I had a large number of representations on this point, including representations from the hon. member for Stanstead who is unable to be here this afternoon. What is being proposed now can be summed up in three statements. First, the base on which premium taxes will be levied in future will be uniform for all classes of insurers, and the basis will be net premiums as distinct from gross premiums. Second, there will be a uniform rate of two per cent applying to all classes of insurers with two exceptions; third, the two exceptions are insurers under Lloyds and reciprocal insurers otherwise known as exchanges. *These two classes, it is believed, will not be subject to corporation income tax in Canada, and because of this fact the premium tax in their case will be three per cent in place of the general two per cent.* I will ask

my colleague, the Minister of National Revenue, to move an amendment to resolutions 4 and 5 \* \* \*.” Dominion of Canada, official Report of Debates House of Commons, second session—Twentieth Parliament—10 George VI, 1946, Vol. IV, 1946, Friday, August 2, 1946, page 4244. (Italics ours)

Referring to the proposed imposition of the tax on farm mutuals the Honorable Mr. Abbott stated as follows:

“I agree that farm mutuals do perform a service and have a type of insurance which most of the stock and other companies are not anxious to take. But there is no real difference in principle or practice between the service they are rendering to their members and that found in a cooperative organization. I do not agree with the hon. member when he says that the tax here is a serious matter. *The heavy and the important tax in connection with ALL these mutuals is the premium tax; there is no doubt about that \* \* \*.*” (Emphasis supplied). Dominion of Canada, official Report of Debates House of Commons, second session, Twentieth Parliament, 10 George VI, 1946, Vol. V, 1946, Tuesday, August 13, 1946, pages 4735, 4736.

On the same date the Honorable Mr. Abbott, referring to the general writing mutuals as well as the farm mutuals, stated as follows:

“The McDougall commission reported that these mutuals (*cash premium mutuals*) should be put on the same basis as other cooperatives. They did suggest, in the case of farm mutuals more than fifty per cent of whose business was insuring farm property, exemption from taxation. The commission says on page 65 (*Italicized portion inserted*):

“‘We are of the opinion that mutuals can and do have income which is subject to tax. This income results from investments and operating gains which are free from claims of policyholders. At the same time we consider that mutuals in certain specialized fields are

rendering a service which is not provided by other organizations, notably, in insuring farm and other unprotected rural risks. These mutuals tend to keep their rates as low as is consistent with the risk involved. We consider that it would not be in the public interest to impose income tax upon those insurers whose activities are primarily in these fields.'

"They recommended that if more than fifty per cent of the business was in insuring farm property they should be exempt. That was considered by the minister and his advisers, and it was felt that we should not single out a special class of insurance companies for complete exemption. *This particular class already receives special treatment by exemption from the premium tax, which is the important tax in this field \* \* \*.*" (Italics ours). Dominion of Canada, official Report of Debates of House of Commons, second session—Twentieth Parliament, 10 George VI, 1946, Vol. V, 1946, Tuesday, August 13, 1946, page 4738.

The following quotations are taken from debates of the Senate of the Dominion of Canada, 1946, official Report, Second Session—20th Parliament—10 George VI, at the end of each quotation is an appropriate reference to the date and page.

On August 15, 1946, the Honorable Mr. Hayden, who presented to the Senate the proposed amendments to the Canadian Special War Revenue Act, stated as follows:

" \* \* \* \* \*

"The first amendment provides for a change in the definition of 'net premiums.' As honourable senators know, the Special War Revenue Act provides for a tax upon premiums received by insurance companies. Up to this year mutual insurance companies in Canada have paid no income tax, and this situation will continue until the amendments to the Income Tax Act are ratified. *The mutual insurance companies were*

*reached through the medium of a tax on premiums.*  
 \* \* \*." Page 645 (Italics ours)

The Honorable W. D. Euler, in 1946, was chairman of the Canadian Senate Committee on Taxation. In debating the amendment to the Canadian Income War Tax Act on August 29, 1946, the Honorable Mr. W. D. Euler stated as follows:

“ \* \* \* \* \*  
 “These small companies—mostly mutual companies doing fire, casualty and other insurance—do not for one moment object to being taxed on their profits. I would like honourable senators to bear in mind that while these companies have been so far subject to a tax on their premiums only and have paid no income tax at all, they never thought that was a right procedure. They have always felt that they should be subject to income tax on their profits, just as any other business concern is, but because *the tax on premiums was practically the same in amount as the income tax would have been*, they raised no particular objection.  
 \* \* \*." (Italics ours). August 29, 1946, page 762.

## APPENDIX No. XXVI

The following quotations contain those subsections of the Special War Revenue Act of 1942 providing penalties for failure to pay the tax or file returns as provided. The quotations are of subsection 20 and 21, Part III, Chapter 179, R.S. 1927, page 8:

20. 1. Every company to which section fourteen or section fifteen of this Act applies which refuses or neglects or whose chief agent or attorney, as the case may be, refuses or neglects to make any return as required by this Part shall be liable to a penalty not exceeding fifty dollars for each and every day during which such refusal or neglect continues.

2. Every president, vice-president, managing direc-



tor, secretary, officer, clerk or servant, agent or attorney of such company, who willfully makes a false or deceptive statement in the return aforesaid or in any of the books and records of the company from which such return is compiled, shall be guilty of an indictable offence punishable, unless a greater punishment is in any case by law prescribed therefor, by imprisonment for a term not exceeding five years.

3. Every president, vice-president, managing director, secretary, officer, clerk or servant, agent or attorney of such company, who negligently prepares or signs a return or record of the company containing a false or deceptive statement or who negligently makes an untrue entry in the books of the company affecting the correctness of the return shall be guilty of an indictable offence punishable, unless a greater punishment is in any case by law prescribed therefor, by imprisonment for a term not exceeding three years.

21. Every person who fails or neglects to make the return required by section eighteen of this Act, or to pay to the Minister within the time limited by section sixteen of this Act, the tax thereby imposed, shall incur a penalty of fifty dollars for each and every day during which such default continues. 1932, c. 54, s. 1; 1942, c. 32, s. 8.



No. 12338

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**In the United States Court of Appeals  
for the Ninth Circuit**

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**NORTHWESTERN MUTUAL FIRE ASSOCIATION,  
PETITIONER**

**v.**

**COMMISSIONER OF INTERNAL REVENUE, RESPONDENT**

---

**ON PETITION FOR REVIEW OF THE DECISION OF THE TAX  
COURT OF THE UNITED STATES**

---

**BRIEF FOR THE RESPONDENT**

---

**THERON LAMAR CAUDLE,**  
*Assistant Attorney General.*

**ELLIS N. SLACK,  
HELEN GOODNER,  
CARLTON FOX,**  
*Special Assistants to the Attorney General.*

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**FILED**

**JAN 16 1950**

**PAUL P. O'BRIEN,**





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**In the United States Court of Appeals  
for the Ninth Circuit**

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No. 12338

NORTHWESTERN MUTUAL FIRE ASSOCIATION,  
PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

---

*ON PETITION FOR REVIEW OF THE DECISION OF THE TAX  
COURT OF THE UNITED STATES*

---

**BRIEF FOR THE RESPONDENT**

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**OPINION BELOW**

The only previous opinion is that of the Tax Court promulgated March 30, 1949 (R. 48-66), which is reported in 12 T.C. 498.

**JURISDICTION**

The petition for review (R. 67-70) involves deficiencies in federal income taxes determined by the Commissioner against the taxpayer, Northwestern Mutual Fire Association, for the taxable years 1942 and 1943, in the amounts of \$5,089.03 and \$5,347.81, respectively. On July 18, 1947, the Commissioner mailed to the taxpayer a notice of deficiency in such taxes in the aggregate amount of \$10,436.84. (R. 14-20.) Within 90 days

thereafter, and on October 14, 1947, the taxpayer filed a petition with the Tax Court of the United States for the redetermination of such deficiencies under Section 272 (a) (1) of the Internal Revenue Code. (R. 4-20.) The decision of the Tax Court that there are deficiencies in income taxes for the years 1942 and 1943 in the respective amounts of \$5,089.03 and \$5,347.81 was entered March 30, 1949. (R. 66.) The proceeding is brought to this Court by a petition for review filed June 24, 1949 (R. 67-71), under the provisions of Section 1141 (a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948.

#### QUESTION PRESENTED

Whether the taxpayer is entitled to a foreign tax credit, under Section 131 of the Internal Revenue Code, in each of the taxable years 1942 and 1943 on account of the Canadian "net premium" tax paid by it in each of those years.

The answer to this question depends upon whether the Canadian "net premium" tax is a tax paid "in lieu of a tax upon income \* \* \* otherwise generally imposed by any foreign country," within the meaning of Section 131 (h) of the Code.

#### STATUTES AND OTHER AUTHORITIES INVOLVED

The statutes and other authorities involved are set out in the Appendix, *infra*.

#### STATEMENT

The findings of fact made by the Tax Court (R. 48-57) are based upon a stipulation of facts (R. 24-42), and may, for the purposes in hand, be summarized as follows:

The deficiencies determined by the Commissioner against the taxpayer, a domestic mutual fire insurance company, are due primarily to the disallowance by the



Commissioner of a foreign tax credit in each of the taxable years 1942 and 1943 on account of a Canadian "net premium" tax paid by the taxpayer in each of those years in the equivalent in terms of United States funds of the sums of \$15,272.16 and \$16,202.54, respectively, under the Special War Revenue Act of 1915, Revised Statutes of Canada of 1927, as amended by the Statutes of Canada of 1942, c. 32, Part III. (R. 48-50.)

The taxpayer's gross income for 1942 and 1943 from all sources was \$6,716,320.72 and \$7,045,067.97, respectively, and its gross income from sources in Canada, in terms of United States funds, was \$507,681.54 and \$533,-987.07, respectively. (R. 51.)

In 1942 and 1943, the taxpayer's "normal-tax net income" from all sources was \$126,451.85 and \$151,828.23, respectively, while for these years its normal-tax net income from sources in Canada, in terms of United States funds, was \$37,843.46 and \$40,943.06, respectively. (R. 52.)

During these years, the taxpayer was not liable on its net income from Canadian business under the provisions of the Canadian Income War Tax Act of 1917, as amended, the provisions of which are set forth in the Revised Statutes of Canada of 1927, c. 97. (R. 52-53.)

Prior to 1942, the taxpayer was required by the provisions of the Special War Revenue Act of 1915, Revised Statutes of Canada of 1927, c. 179, to pay to the Dominion of Canada a tax of one percent on its net premiums from its business within Canada. In 1942, an Act to Amend the Special War Revenue Act of 1915, Statutes of Canada of 1942, c. 32, increased the "net premium" tax on all fire insurance companies doing business in Canada, including the taxpayer. For all mutual fire insurance companies, such as the taxpayer, not subject to taxation on their net income under the Income War Tax Act of 1917, the rate was increased

from one to three percent. For all fire insurance companies which were subject to the Canadian tax on their net income under the Income War Tax Act of 1917, which did not include the taxpayer, the rate was increased from one to two percent. (R. 53-54.)

In 1946, mutual fire insurance companies, including the taxpayer, were made subject to the general income tax laws of Canada by an Act to Amend the Income War Tax Act of 1917, Statutes of Canada of 1946, c. 55. (R. 54.)

Concurrent with the above noted changes in the Income War Tax Act of 1917, the Special War Revenue Act of 1915, as amended in 1942, was amended further by an Act to Amend the Special War Revenue Act of 1915, Statutes of Canada of 1946, c. 65, Sec. 2, so as to reduce the rate of the tax from three to two percent. (R. 55.)

In 1942 and 1943, the taxes imposed by the Special War Revenue Act of 1915, as amended, as well as by the Income War Tax Act of 1917, as amended, were paid to the Minister of National Revenue, sometimes referred to as the Finance Minister. In these years, the administrative details of collection and auditing of taxes payable by insurance companies under the Special War Revenue Act of 1915, as amended, as well as the auditing of income tax returns of insurance companies which were subject to the provisions of the Income War Tax Act of 1917, as amended, were handled by the Department of Insurance. However, in those years, the details of collection and auditing of taxes other than taxes on insurance companies payable under the Special War Revenue Act were handled by the Department of National Revenue. (R. 56.)

In its returns for 1942 and 1943, the taxpayer used as a basis for computing its foreign tax credit under Section 131, the ratio of its gross income from Canada to

its total gross income in each of those years and thus computed its credit for 1942 in the amount of \$5,076.60 and for 1943 in the amount of \$5,339.84. However, in its claims for refund for those years, it computed its credit for each year on the basis of the ratio of its "normal-tax net income" from sources in Canada to its "normal-tax net income" from all sources.<sup>1</sup> (R. 56-57.)

The Tax Court held that the taxpayer was not entitled to the credit claimed by it in either year and accordingly sustained the Commissioner's deficiency determination. (R. 65-66.)

#### SUMMARY OF ARGUMENT

Whether the taxpayer is entitled to a foreign tax credit under Section 131 of the Internal Revenue Code in each of the taxable years 1942 and 1943 on account of the Canadian "net premium" tax paid by it in each of those years depends upon whether such tax is a tax paid "in lieu" of a tax on net income, within the meaning of subsection (h) of that section, which was added to the Code by Section 158 of the Revenue Act of 1942. We first discuss the facts in the light of the applicable federal and Canadian statutes under our subpoint A, and then, under our subpoint B, the question whether the Canadian "net premium" tax is one paid by the taxpayer "in lieu" of a tax on income, otherwise generally imposed by the Dominion of Canada, within the meaning of Section 131 (h).

A. The taxpayer, a mutual fire insurance company, had net investment income in 1942 and 1943 both from sources within the United States and from sources within Canada, which was subject to an income tax in

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<sup>1</sup> It may here be noted that, under Section 207 (b)(4), the "normal-tax net income" of mutual insurance companies, including the taxpayer, was their investment income, which was subjected to the income tax by subsection (a)(1)(A) and (B) of that section.



the United States under Section 207 of the Code, as amended by Section 165 of the Revenue Act of 1942. In the taxable years here in question, mutual insurance companies were exempt from the Canadian income tax, but were subject to a so-called "net premium" tax in Canada. Section 207 (a)(1) of the Internal Revenue Code imposes an income tax at the rate of 30 percent upon the taxpayer's total net investment income. Alternatively, subsection (a)(2) of the section imposes a "special tax" of one percent upon the gross amount of its investment and "net premium" income, provided that such "special tax" is greater than the tax upon the net investment income. In the case at bar, the "special tax" was the greater in each year. Consequently, the amount thereof was assessed and paid in each year. The Canadian "net premium" tax is a business privilege or franchise tax, rather than an income tax, within the meaning of the term "income tax" used in Section 131 of the Code, which grants a credit on account of foreign taxes described therein and to the extent therein provided. While, in its income tax returns for 1942 and 1943, the taxpayer computed a foreign tax credit for each year on the gross amount of its net income for each year, as defined by Section 207 (b) (1), before the Tax Court it claimed, as it claims here and therefore concedes, that the basis to be used is the ratio of its "normal-tax net income," that is, its investment income, in Canada to its entire "normal-tax net income," as provided in Section 131 (b)(1). Since the taxpayer concedes that it is not entitled to the credit unless it is entitled thereto under Section 131 (h), the sole question here presented is whether the Canadian "net premium" tax is "a tax paid *in lieu of a tax upon net income* \* \* \* otherwise generally imposed by any foreign country" within the meaning of that section. (Italics supplied.)



B. The critical words in Section 131 (h) are the words "in lieu of a tax upon income." It is well settled that, in the application of Section 131, the criteria of the federal and not the criteria of the foreign laws determine the meaning of the term "income taxes." It follows that, in determining what is a tax "in lieu of a tax upon income," the criteria of the federal and not of the Canadian laws are determinative. In any event, an inquiry into the Canadian purpose is illusory, and is, at best, merely an inquiry into a question of fact. Such inquiry is, therefore, obviously foreclosed by the Tax Court's finding against the taxpayer. The taxpayer's contention that Congress had the Canadian "net premium" tax specifically in mind when it enacted Section 131 (h) has nothing whatever to support it; so, also, the taxpayer's contention that Congress intended thereby to overrule the administrative and judicial decisions holding that it was not an income tax. Indeed, the contrary appears from the Senate Report, for this report states that Section 131 (h) was designed to give relief in cases where the foreign country which imposes income taxation, and which, because of administrative difficulties in determining either net income or taxable basis, authorizes an American company doing business therein to pay a tax, in lieu of an income tax, *measured* by gross income or gross sales, or number of units produced, or by some other method which is the equivalent of the income tax. But Canada had no such difficulty. It just did not impose an income tax upon the investment income of mutual insurance companies, or upon any other income of such companies in 1942 and 1943, though it did later in 1946. And it imposed no tax "in lieu" thereof, in the sense that it imposed no other tax in respect of a mutual insurance company's investment income or investment business, however measured. Moreover, the Senate Report cautions that the limita-

tion provisions of Section 131 remain applicable. Therefore, what we are looking for here is a Canadian tax upon investment income, measured in some other way than by an income tax upon the net amount thereof. The requirements of Section 131 (h) are satisfied only so long as there is a direct relationship between the Canadian exaction and the American tax base. Such, for example, would be a tax upon the taxpayer's gross investment income, as indicated, or upon its doing an investment business, or upon the holding of investments by it, measured by their value. Conceivably, there may be other ways of measuring such a tax; but, by definition, a tax upon "net premiums" is obviously not one of these.

#### ARGUMENT

#### **The Taxpayer Is Not Entitled to a Foreign Tax Credit in Each of the Taxable Years 1942 and 1943 on Account of the Canadian "Net Premium" Tax Paid by It in Each of Those Years**

In this case, it is exceedingly important that the facts be understood in the light of both the applicable federal and Canadian statutes. We have, therefore, divided our argument into two parts. Under our subpoint A we shall discuss the facts in their relation to these statutes, leaving to our subpoint B the argument upon the sole question here involved, namely, whether the Canadian "net premium" tax is one which was paid by the taxpayer "in lieu of a tax upon income," otherwise imposed by the Dominion of Canada, within the meaning of Section 131 (h) of the Internal Revenue Code, as added thereto by Section 158 (f) of the Revenue Act of 1942 (*Appendix, infra*).

#### *A. The facts in their relation to the provisions of both the federal and Canadian statutes*

The taxpayer is a domestic mutual fire insurance company which did a business as such in the taxable

years 1942 and 1943 both in the United States and in Canada. During these years, it had a total net investment income of \$126,451.85 and \$151,828.23, respectively, of which \$37,843.46 was derived from sources in Canada in 1942 and \$40,943.06 in 1943.

In these years, the taxpayer was exempt from the Canadian income tax upon its Canadian income, including its investment income by the Income War Tax Act of 1917, Revised Statutes of Canada of 1927, c. 97. (R. 53.) On the other hand, it was subject to a federal income tax imposed upon its entire investment income, derived both from sources in the United States and from sources in Canada, under Section 207 of the Internal Revenue Code, as amended by Section 165 of the Revenue Act of 1942 (Appendix, *infra*).

Subsection (b)(4) of Section 207 defines the "net income" of a mutual insurance company as its "gross investment income," less tax-free interest, investment expenses, real estate expenses, depreciation, interest paid or accrued, and capital losses. In passing, it may be noted that "net income," as thus defined, is referred to in subsection (a)(1)(A) and (B) of Section 207, which imposes the income tax thereon, as "normal-tax net income," and that this is likewise the designation given thereto in Section 131 (b)(1), as amended by Section 130 of the Revenue Act of 1943 (Appendix, *infra*), which, as hereinafter explained, contains the credit limitation provisions. For the definition of "normal-tax net income" see Section 13 (a)(1) and (2) (Appendix, *infra*). Subsection (b)(1) of Section 207 defines the "gross investment income" of such company to be the gross amount of income derived by it during the taxable year from interest, dividends, rents, and gains from sales or exchanges of capital assets to the extent provided in Section 117.



By subsection (a)(1)(A) of Section 207, already referred to, a normal tax of 30 percent is imposed upon the company's "normal-tax net income" (subject to a qualification not here important), that is, upon its "net income" as defined by subsection (b)(4); and, by subsection (a)(1)(B), a surtax of 20 per cent is imposed upon its surtax net income, as defined by Section 15 (a) of the Code (Appendix, *infra*). However, alternatively, a "special tax"<sup>2</sup> of one percent, or, in circumstances not material here, of two percent, is imposed by subsection (a)(2) (if such special tax is greater than that imposed by subsection (a)(1)), upon the "gross amount of income," exceeding \$75,000 during the taxable year, derived from interest, dividends, rents, and net premiums, minus dividends to policyholders, minus interest which is excluded from gross income under Section 22 (b)(4), and less the amount of the excess profits tax imposed under Subchapter E of Chapter 2 of the Code.

"Net premiums" are defined by subsection (b)(2) of Section 207 to mean gross premiums (including deposits and assessments) written or received on insurance contracts during the taxable year, less return premiums and premiums paid or incurred for reinsurance. And "dividends to policyholders" are defined by subsection (b)(3) to be dividends and similar distributions paid or declared to policyholders, the term "paid or declared" to be construed in accordance with the method regularly employed by the insurance company in keeping its books.

In the case at bar, the income tax upon the taxpayer's net investment income under subsection (a)(1) of Section 207, was \$55,635.87, and the "special tax" upon the

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<sup>2</sup> So called in S. Rep. No. 1631, 77th Cong., 2d Sess., p. 151 (1942-2 Cum. Bull. 504, 615-616).



gross amount of its income under subsection (a) (2) was \$67,150.78. Thus, since the tax computed upon the taxpayer's gross amount of income in the taxable year 1942 was larger by \$11,514.91 than that computed upon its net investment income, its tax liability under Section 207 for that year was the larger amount. (Pet. Ex. 1-A.) And, since the income tax upon the taxpayer's net investment income under subsection (a) (1) of Section 207, as reported for the taxable year 1943, was \$65,385.01, and upon the gross amount of its income under subsection (a) (2), \$70,442.71, here too, the "special tax" computed on the taxpayer's gross amount of income was greater, by \$5,057.70, than that computed upon its net investment income, and its tax liability under Section 207 for 1943 was in the larger amount. (Pet. Ex. 6-F.)

In 1942, the taxpayer's "net premiums," as defined by the Canadian War Revenue Act of 1915, as amended by an Act to Amend the Special War Revenue Act of 1915, Statutes of Canada of 1942, c. 32, Part III, to consist of gross premiums in Canada less rebates and return premiums and reinsurance premiums ceded to licensed companies (R. 50-51), amounted to \$559,979.69 (Pet. Ex. 5-E), and in 1943 to \$594,094.51 (Pet. Ex. 10-J). The "net premium" tax which the taxpayer paid to the Dominion of Canada in 1942 under that Act was \$15,495.48, and in 1943, \$17,822.81. This tax has been held to be a business privilege or franchise tax, rather than an income tax, within the meaning of the term "income tax" as used in Section 131 of the Code (Appendix, *infra*), which embodies the foreign tax credit provisions thereof. I.T. 3188, 1937-2 Cum. Bull. 230; *Continental Insurance Co. v. Commissioner*, 40 B.T.A. 540; *St. Paul Fire & Marine Ins. Co. v. Reynolds*, 44 F. Supp. 863 (Minn.); *Helvering v. Queen Ins. Co.*, 115 F.2d 341 (C.A. 2d); cf. I.T. 3211, 1938-2 Cum. Bull.

177, involving similar "net premium" taxes of the Canadian provinces.

In its returns for each of the taxable years 1942 and 1943, the taxpayer claimed a credit under Section 131 of the Code on account of the amount of "net premium" tax it had paid the Dominion of Canada in each year. The amount of the credit claimed for 1942 was \$5,076.60, and that for 1943 \$5,339.84. Such amounts were computed under the limitation provisions of Section 131 (b)(1), already referred to. But the taxpayer computed the credit in its returns on the gross amount of income for each year, as defined by Section 207(a)(2). (R. 56-57.) However, before the Tax Court, the taxpayer claimed, as it claims here and thus concedes (Br. 80-81), that, in computing such credit under Section 131(b)(1), the ratio to be used is the taxpayer's "normal-tax net income" in Canada to its entire "normal-tax net income", upon which the income tax was imposed under Section 207(a)(1)(A) and (B), as stated. In other words, the taxpayer's foreign tax credit, if any, is concededly limited by Section 131(b)(1) to an amount represented by the ratio which its net investment income in Canada bears to its entire net investment income.

The taxpayer concedes that it is not entitled to the credit on account of the Canadian "net premium" tax which it paid unless it is entitled thereto in virtue of subsection (h) of Section 131, already referred to, because that tax is not an income tax. However, subsection (h) allows the credit for a tax paid "in lieu" of such a tax, and the taxpayer claims that the Canadian "net premium" tax qualifies as such under that subsection. Whether it does or not is, therefore, the sole question in this case and we shall address ourselves thereto.

B. *The Canadian "net premium" tax is not "a tax paid in lieu of a tax upon income \* \* \* otherwise generally imposed by any foreign country," within the meaning of Section 131 (h) of the Code.*

Section 131 (h) provides as follows:

(h) *Credit for Taxes in Lieu of Income, Etc., Taxes.*—For the purposes of this section and section 23 (c) (1), the term "income, war-profits, and excess-profits taxes" shall include a tax paid *in lieu of a tax upon income*, war-profits, or excess-profits otherwise generally imposed by any foreign country or by any possession of the United States. (Italics supplied.)

The critical words, of course, are the words "in lieu of a tax upon income."

It is now well settled that, in the application of Section 131, the criteria presented by our own revenue laws and court decisions, and not by those of foreign laws, control the meaning of the term "income taxes," as used therein. *Biddle v. Commissioner*, 302 U. S. 573, 578, 579; *Keasby & Mattison Co. v. Rothensies*, 133 F. 2d 894, 897 (C.A. 3d), certiorari denied, 320 U. S. 739; *New York & H. Rosario Min. Co. v. Commissioner*, 168 F. 2d 745 (C.A. 2d); *H. H. Robertson Co. v. Commissioner*, 176 F. 2d 704 (C.A. 3d).

It follows that, since Section 131 (h) merely assimilates to a foreign tax paid on income, in respect of which the credit is allowed, a foreign tax paid "in lieu" thereof, what is such an "in lieu" tax depends upon our own, and not upon the foreign law. It is, therefore, wholly beside the point to argue, as the taxpayer does, that, under Canadian law, and particularly in the light of the legislative history of the amendments of the Canadian "net premium" tax and of the enactment of other more or less related tax measures, a conclusion is

admissible that Canada intended to impose or to retain such tax "in lieu" of an income tax upon the taxpayer's net investment income.

In any event, an inquiry into the purpose of the Canadian Parliament to impose, or to retain, a "net premium" tax in lieu of an income tax upon the taxpayer's net investment income is not only illusory, but is preeminently an inquiry into a question of fact, and the Tax Court, upon a view of all the facts, has already answered that question against the taxpayer's contention. Therefore, whether the "net premium" tax is one which Canada intended to impose or retain as a substitute for an income tax upon the taxpayer's net investment income, if relevant, is, we submit, a question which is not open to review here, for the evidence is by no means so conclusive as to justify a conclusion that it was. To the contrary, the answer to that question depends wholly upon the weighing of conflicting inferences which may be drawn from the evidence; and certainly, the fact that in 1946 Canada imposed a tax upon the net income of mutual insurance companies while retaining the "net premium" tax is ample evidence that Canada neither imposed nor retained the "net premium" tax as a substitute for the income tax.

Nor is the taxpayer's argument (Br. 38) persuasive that, in enacting the provisions of Section 131 (h), Congress expressly intended to permit a credit on account of this particular Canadian tax, on the theory that it satisfied the requirement of a tax imposed in lieu of the federal income tax and that, to this end (Br. 29-31), Congress intended legislatively to overrule not only the administrative rulings holding that such tax was not an income tax within the meaning of the federal law, but the decisions of both the Tax Court and the federal courts, as well, and particularly the decision of the United States District Court for the District of Minne-



sota in the case of *St. Paul Fire & Marine Ins. Co. v. Reynolds*, 44 F. Supp. 863.

The best that can be said is that, generally speaking, Congress had the whole field of foreign taxation in mind and knew that gains, profits and income, from whatever source derived, were at times, due to administrative difficulties in determining either net income or taxable basis, subjected to taxes in foreign countries which differed from the conventional federal income tax. Congress recognized that, nonetheless, such taxes involved the imposition of a double tax on the taxpayer's income when it was also subjected to the federal income tax. But he would be venturesome, indeed, who essayed to cull from the multitude of existing Bureau of Internal Revenue rulings, both published and unpublished, or from the multitude of cases decided by it without special rulings, those against which the amendment was specifically directed. What is made clearly to appear, however, from the Senate Report already referred to, namely, S. Rep. No. 1631, p. 131 (1942-2 Cum. Bull. 504, 602), is that Section 131 (h) was designed to give relief where, as stated, the foreign country which imposed "income taxation"—i.e., an income tax on income which was also subject to the federal tax—because of the administrative difficulties of determining net income or taxable basis, authorized an American domestic corporation doing business in that country to pay, as a substitute for the income tax otherwise imposed, a tax *measured* by gross income, gross sales, number of units produced, or by some other method which was the equivalent of the "income tax" otherwise imposed by such country. Of course, the evidence here does not disclose that Canada originally imposed, or that it later retained, the "net premium" tax because of any administrative difficulty in determining either the gross or net investment income of a

mutual insurance company, to be used as a base for the tax. Canada just did not impose a tax upon the net investment income of such companies, or upon their gross investment income, or any other kind of tax, in respect of their investment income or business.

In this connection, it is to be noted that the Senate Report referred to cautions that the limitation upon the amount of the credit will, of course, continue to apply, so that the credit is granted only to the extent that the taxpayer has net income from sources within the foreign country.

Thus in order to carry out the Congressional intent, what we must look for is a Canadian tax based upon investment income, however measured. In other words, the requirements of Section 131 (h) are satisfied only if the exaction has a direct relationship to the American tax base, such, for example, as a tax upon gross investment income, or a tax upon the doing of an investment business, or a tax upon the holding of investments measured by their value. For, while any of these taxes would not satisfy the technical criteria of the federal income tax, it would obviously satisfy the criteria of a tax levied "in lieu" thereof; and, at the same time, it would, of course, also satisfy the criteria of the tax base used in the limitation provisions of subsection (b)(1) of Section 131.

Moreover, it is only by so construing Section 131 (h) that a true relationship is established between the federal and the foreign tax and the object of the statute attained. Thus, and thus only, is subsection (h) brought into harmony with both subsections (a) and (b) of Section 131. On the other hand, diametrically the opposite is true if Section 131 (h) is construed as the taxpayer contends it should be. As stated, if the Canadian tax on net premiums is allowed as a credit, it can admittedly be allowed only to the extent that

the taxpayer has taxable gross investment income from Canadian sources which could be reduced to net investment income by applying federal tax provisions, the credit being limited, of course, as provided in Section 131 (b) (1). Thus, if, for example, the taxpayer had no investment income in Canada, it would obviously not be entitled to any credit on account of the Canadian "net premium" tax. Only if the Canadian "net premium" tax were substituted as the numerator and the gross amount of income determined under Section 207 (a) (2) were substituted as the denominator in the ratio provided for in the limitation provisions of Section 131 (b) (1) (which the taxpayer, however, no longer claims to be proper), would it be possible to bring the allowance of a credit on account of the Canadian "net premium" tax, as an "in lieu" tax within the meaning of Section 131 (h), into harmony with the limitation provisions of Section 131 (b) (1). Indeed, the very fact that such substitution is not permissible under Section 131 (b) (1) is the basis of the Commissioner's additional reason for disallowing the credit, which is that "a proper application of the provisions of Section 131 of the Internal Revenue Code negatives the use of investment income as the basis for computing the limitation factor provided for under subsection (b) thereof, in the case of a mutual insurance company (other than life or marine) paying a tax based upon 'the gross amount of income' as defined in Section 207 of the Internal Revenue Code." (R. 17.)

The taxpayer's contention (Br. 18-20) that Section 29.131-2 of Treasury Regulations 111 (Appendix, *infra*), inadvertently referred to by the taxpayer as Treasury Regulations 103, supports a contrary view is wholly without merit. It will be noted that these Regulations stress the fact referred to in S. Rep. No. 1631, *supra*, that the reason for the amendment lay in



the administrative difficulties a foreign country might have in determining net income, when it would, however, have no difficulty in determining gross income. Consequently, the Regulations say, also following the language of the Senate Report, that the tax might be laid, for example, on gross income and thus qualify for a credit under Section 131 (a). But we look in vain to the Regulations to justify the grant of the credit on account of a foreign excise tax levied on mutual insurance companies in respect of "net premiums" derived from its insurance business in the foreign country.

And this also disposes of the taxpayer's contention (Br. 35-36) that, because, in this case, the amount of the tax was alternatively computed on the gross amount of the income, including the total of "net premiums," a double tax was imposed upon Canadian "net premiums," which Congress sought to obviate by Section 131 (h). The specific answer to this contention, of course, is that the alternative "special tax" was designed merely to produce a larger tax in certain cases than that produced by the tax upon taxable net income as defined by Section 207 (b)(4). In the case at bar, this is the taxpayer's net investment income, which does not, of course, include "net premium" income. The result is that only the excess of the tax on the taxpayer's gross amount of income, imposed under Section 207 (a)(2), over the tax on its net investment income, imposed under Section 207 (a)(1), is properly attributable to the imposition of the "special tax."

But such excess, together with the method of taxation by which it was arrived at, was deliberately disregarded by Congress in fixing the basis for the credit and its limitation under Section 131 (b). Obviously, if Congress had intended that a credit for the Canadian "net premium" tax should be allowed against the "special tax," because the Canadian "net premiums" were



included in the "special tax" base, it could, and unquestionably would, have specifically so provided in Section 131 (h). In this connection it may be noted that Section 207 (a)(2), imposing the special tax, was enacted in the Revenue Act of 1942, as was Section 131 (h). Thus, had the House amendment of Section 207 been enacted into law, instead of the Senate's substitution therefor, it might with force have been argued that, if subsection (h) had in that situation been added, the Canadian "net premium" tax was a tax paid "in lieu" of the income tax imposed upon mutual insurance companies. And the taxpayer might well have referred in support thereof to the quotation from the House Report (H. Rep. No. 2333, 77th Cong., 2d Sess., pp. 27-28 (1942-2 Cum. Bull. 372, 395)) which it makes without apparent application in its Appendix No. VII (Br. p. marked "Appendix 8"). See also the same report, pp. 113-118 (1942-2 Cum. Bull. 372, 456-460). Under the House amendment,<sup>3</sup> mutual insurance companies were taxed on their entire net income, including "net premiums," which were similarly defined as in the Canadian act.

Instead, Congress adopted the Senate amendments of Section 207, which, as stated, imposed an income tax upon the net investment income of mutual insurance companies, and only alternatively the "special tax" on the amount of gross income, if that was larger. At the same time, however, by its 1942 amendment of Section 131 (a)(1), the foreign tax credit was not expanded by subsection (h) to include a tax on "net premium" income, but only to include a tax imposed "in lieu" of net income tax, i.e., in this case, in lieu of an income tax on "net investment" income, such as

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<sup>3</sup> For the convenience of the Court, the provisions of the House bill as it was reported to and as it passed the House, which are identical, are set out in full at the end of the Appendix, *infra*.

a tax upon gross investment income, or, perchance, a tax laid in respect of the doing of an investment business, measured by the value of the investments.

Thus, under Section 131 (a)(1), as amended by Section 158 (a) of the Revenue Act of 1942, a credit was allowed in respect of any income, war profits, or excess profits taxes paid by a corporation to any foreign country, and by Section 131 (b)(1), as first amended by Section 158 (d) of the 1942 Act, the credit was limited by the ratio which the corporation's net income from sources within such country bore to the sum of its "normal-tax net income" and the amount of the credit for adjusted excess profits tax income provided in Section 26 (e) of the Code, for the same year. Moreover, when by Section 130 (b)(1) of the Revenue Act of 1943 Congress again amended Section 131 (b)(1) retroactively to years beginning after December 31, 1939, it provided that the corporation's credit should be limited by the same proportion of the tax against which the credit is taken, which its "normal-tax net income" from sources within the foreign country bears to its entire "normal-tax net income" for the same taxable year. The Senate Report, S. Rep. No. 627, 78th Cong., 1st Sess., pp. 62-64 (1944 Cum. Bull. 973, 1019-1020), elaborately explains that the reason for this amendment was properly to reflect foreign dividends in the credit of certain corporations.

Thus, nowhere is there the slightest indication that Congress intended by Section 131 (h) to permit the inclusion in the credit base of anything but "normal-tax net income," or to allow the credit to be taken on account of a foreign tax which was not levied in respect of such base.

It seems to us, therefore, that what we have said demonstrates that Congress did not intend Section 131 (h) to apply to the Canadian "net premium" tax.

The foregoing analysis also shows, we think, that the taxpayer's reliance upon authorities which hold taxing statutes, and particularly the remedial provisions thereof, should be liberally construed in the taxpayer's favor, is wholly misplaced. We are here to determine what the construction of Section 131(h) should fairly be; that is to say, to fairly delimit the relief thereby granted. This is not at all impossible, as we have seen, without the resort to a rule of thumb, such as that which the taxpayer seeks to apply, and which, in any event, would be available, if at all, as an aid in construction only when all other rules of construction fail. As Mr. Justice Stone said in *White v. United States*, 305 U. S. 281, 292—

We are not impressed by the argument that, as the question here decided is doubtful, all doubts should be resolved in favor of the taxpayer. It is the function and duty of courts to resolve doubts. We know of no reason why that function should be abdicated in a tax case more than in any other where the rights of suitors turn on the construction of a statute and it is our duty to decide what that construction fairly should be. Here doubts which may arise upon a cursory examination of §§ 101 and 115 disappear when they are read, as they must be, with every other material part of the statute, *Hellmich v. Hellman*, *supra*, 237, and in the light of their legislative history. Moreover, every deduction from gross income is allowed as a matter of legislative grace, and "only as there is clear provision therefor can any particular deduction be allowed . . . a taxpayer seeking a deduction must be able to point to an applicable statute and show that he comes within its terms." *New Colonial Ice Co. v. Helvering*, 292 U. S. 435, 440.

Similarly, we are here dealing with a credit against the tax, which is allowed only as a matter of legislative grace, and the provisions granting credits, like

those granting exemptions and deductions, are strictly to be construed, so that it is incumbent upon the taxpayer seeking the credit to show that he clearly comes within the provisions of the statute allowing it. See *Helvering v. Northwest Steel Mills*, 311 U. S. 46, 47; *United States v. Stewart*, 311 U. S. 60, 71; *Deputy v. du Pont*, 308 U. S. 488, 495; *New Colonial Co. v. Helvering*, 292 U. S. 435, 440.

#### CONCLUSION

For the reasons stated, the decision of the Tax Court should be affirmed.

Respectfully submitted,

THERON LAMAR CAUDLE,  
*Assistant Attorney General.*

ELLIS N. SLACK,

HELEN GOODNER,

CARLTON FOX,

*Special Assistants to the Attorney General.*

JANUARY, 1950.



## APPENDIX

## Internal Revenue Code:

## SEC. 13. TAX ON CORPORATIONS IN GENERAL.

(a) [as amended by Sec. 201 of the Revenue Act of 1939, c. 247, 53 Stat. 862, and Sec. 105 of the Revenue Act of 1942] *Definitions*.—For the purposes of this chapter—

(1) *Adjusted net income*.—The term “adjusted net income” means the net income minus the credit provided in section 26 (a), relating to interest on certain obligations of the United States and Government corporations.

(2) *Normal-tax net income*.—The term “normal-tax net income” means the adjusted net income minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26 (e) and minus the credit for dividends received provided in section 26 (b).

\*                      \*                      \*                      \*

(26 U.S.C. 1946 ed., Sec. 13)

SEC. 15 [as amended by Sec. 104 (a) of the Revenue Act of 1941, c. 412, 55 Stat. 687, and Sec. 105 (b) of the Revenue Act of 1942]. SURTAX ON CORPORATIONS.

(a) *Corporation surtax net income*.—For the purposes of this chapter, the term “corporation surtax net income” means the net income minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26(e) and minus the credit for dividends received provided in section 26 (b) (computed limiting such credit to 85 per centum of the net income reduced by the credit for income subject to the tax imposed by Subchapter E of Chapter 2 in lieu of 85 per centum of the adjusted net income so reduced), and minus, in the case of a public utility, the credit for dividends paid on its preferred stock provided in section 26 (h). For the purposes of this subsection

dividends received on the preferred stock of a public utility shall be disregarded in computing the credit for dividends received provided in section 26 (b).

\* \* \* \* \*

(26 U.S.C. 1946 ed., Sec. 15.)

# SEC. 131. TAXES OF FOREIGN COUNTRIES AND POSSESSIONS OF UNITED STATES.

(a) [as amended by Section 158 (a) of the Revenue Act of 1942]. *Allowance of Credit.*—If the taxpayer chooses to have the benefits of this section, the tax imposed by this chapter, except the tax imposed under section 102 or section 450, shall be credited with:

(1) *Citizens and Domestic Corporations.*—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States; \* \* \*

(b) [as amended by Section 130 (a) of the Revenue Act of 1943]. *Limit on Credit.*—The amount of the credit taken under this section shall be subject to each of the following limitations:

(1) The amount of the credit in respect of the tax paid or accrued to any country shall not exceed, in the case of a taxpayer other than a corporation, the same proportion of the tax against which such credit is taken, which the taxpayer's net income from sources within such country bears to his entire net income for the same taxable year, or in the case of a corporation, the same proportion of the tax against which such credit is taken, which the taxpayer's normal-tax net income from sources within such country bears to its entire normal-tax net income for the same taxable year; \* \* \*

\* \* \* \* \*

(h) [as added by Section 158 (f) of the Revenue Act of 1942]. *Credit for Taxes in Lieu of Income, Etc., Taxes*.—For the purposes of this section and section 23 (c) (1), the term “income, war-profits, and excess-profits taxes” shall include a tax paid in lieu of a tax upon income, war-profits, or excess-profits otherwise generally imposed by any foreign country or by any possession of the United States. (26 U.S.C. 1946 ed., Sec. 131.)

SEC. 207 [as amended by Section 165 (b) of the Revenue Act of 1942]. **MUTUAL INSURANCE COMPANIES OTHER THAN LIFE OR MARINE.**

(a) *Imposition of Tax*.—There shall be levied, collected, and paid for each taxable year upon the income of every mutual insurance company (other than a life or a marine insurance company and other than an interinsurer or reciprocal underwriter) a tax computed under paragraph (1) or paragraph (2) whichever is the greater and upon the income of every mutual insurance company (other than a life or a marine insurance company) which is an interinsurer or reciprocal underwriter, a tax computed under paragraph (3):

(1) If the corporation surtax net income is over \$3,000 a tax computed as follows:

(A) *Normal Tax*.—A normal tax on the normal-tax net income, computed at the rates provided in section 13 or section 14 (b), or 30 per centum of the amount by which the normal-tax net income exceeds \$3,000, whichever is the lesser; plus

(B) *Surtax*.—A surtax on the corporation surtax net income, computed at the rates provided in section 15 (b), or 20 per centum of the amount by which the corporation surtax net income exceeds \$3,000, whichever is the lesser.

(2) If for the taxable year the gross amount of income from interest, dividends, rents, and

net premiums, minus dividends to policy holders, minus the interest which under section 22 (b) (4) is excluded from gross income, exceeds \$75,000, a tax equal to the excess of—

(A) 1 per centum of the amounts so computed, or 2 per centum of the excess of the amount so computed over \$75,000, whichever is the lesser, over

(B) the amount of the tax imposed under Subchapter E of Chapter 2.

(3) In the case of an interinsurer or reciprocal underwriter, if the corporation surtax net income is over \$50,000 a tax computed as follows:

(A) *Normal Tax*.—A normal tax on the normal-tax net income, computed at the rates provided in section 13 or section 14 (b), or 48 per centum of the amount by which the normal-tax net income exceeds \$50,000, whichever is the lesser; plus

(B) *Surtax*.—A surtax on the corporation surtax net income, computed at the rates provided in section 15 (b), or 32 per centum of the amount by which the corporation surtax net income exceeds \$50,000, whichever is the lesser.

(4) *Gross Amount Received Over \$75,000 But Less than \$125,000*.—If the gross amount received during the taxable year from interest, dividends, rents, and premiums (including deposits and assessments) is over \$75,000 but less than \$125,000, the amount ascertained under paragraph (1), paragraph (2) (A), and paragraph (3) shall be an amount which bears the same proportion to the amount ascertained under such paragraph, computed without reference to this paragraph, as the excess over \$75,000 of such gross amount received bears to \$50,000.

(5) *Foreign Mutual Insurance Companies Other Than Life or Marine*.—In the case of a for-



eign mutual insurance company (other than a life or marine insurance company), the net income shall be the net income from sources within the United States and the gross amount of income from interest, dividends, rents, and net premiums shall be the amount of such income from sources within the United States.

(6) *No United States Insurance Business.*—Foreign mutual insurance companies (other than a life or marine insurance company) not carrying on an insurance business within the United States shall not be taxable under this section but shall be taxable as other foreign corporations.

(b) *Definition of Income, Etc.*—In the case of an insurance company subject to the tax imposed by this section—

(1) *Gross Investment Income.*—“Gross investment income” means the gross amount of income during the taxable year from interest, dividends, rents, and gains from sales or exchanges of capital assets to the extent provided in section 117;

(2) *Net Premiums.*—“Net premiums” means gross premiums (including deposits and assets) written or received on insurance contracts during the taxable year less return premiums and premiums paid or incurred for reinsurance. Amounts returned where the amount is not fixed in the insurance contract but depends upon the experience of the company or the discretion of the management shall not be included in return premiums but shall be treated as dividends to policyholders under paragraph (3);

(3) *Dividends To Policyholders.*—“Dividends to policyholders” means dividends and similar distributions paid or declared to policyholders. The term “paid or declared” shall be construed according to the method regularly employed in keeping the books of the insurance company;

(4) *Net Income*.—The term “net income” means the gross investment income less—

(A) *Tax-free Interest*.—The amount of interest which under section 22 (b) (4) is excluded for the taxable year from gross income;

(B) *Investment Expenses*.—Investment expenses paid or accrued during the taxable year. If any general expenses are in part assigned to or included in the investment expenses, the total deduction under this subparagraph shall not exceed one-fourth of 1 per centum of the mean of the book value of the invested assets held at the beginning and end of the taxable year plus one-fourth of the amount by which net income computed without any deduction for investment expenses allowed by this subparagraph, or for tax-free interest allowed by subsection (b) (4) (A), exceeds  $3\frac{3}{4}$  per centum of the book value of the mean of the invested assets held at the beginning and end of the taxable year;

(C) *Real Estate Expenses*.—Taxes and other expenses paid or accrued during the taxable year exclusively upon or with respect to the real estate owned by the company, not including taxes assessed against local benefits of a kind tending to increase the value of the property assessed, and not including any amount paid out for new buildings, or for permanent improvements or betterments made to increase the value of any property. The deduction allowed by this paragraph shall be allowed in the case of taxes imposed upon a shareholder of a company upon his interest as shareholder, which are paid or accrued by the company without reimbursement from the shareholder, but in such cases no deduction shall be allowed the shareholder for the amount of such taxes;

(D) *Depreciation*.—A reasonable allowance, as provided in section 23 (1), for the exhaus-

tion, wear and tear of property, including a reasonable allowance for obsolescence;

(E) *Interest Paid or Accrued*.—All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from taxation under this chapter.

(F) *Capital Losses*.—Capital losses to the extent provided in section 117 plus losses from capital assets sold or exchanged in order to obtain funds to meet abnormal insurance losses and to provide for the payment of dividends and similar distributions to policyholders. Capital assets shall be considered as sold or exchanged in order to obtain funds to meet abnormal insurance losses and to provide for the payment of dividends and similar distributions to policyholders to the extent that the gross receipts from their sale or exchange are not greater than the excess, if any, for the taxable year of the sum of dividends and similar distributions paid to policyholders, losses paid, and expenses paid over the sum of interest, dividends, rents, and net premiums received. In the application of section 117 (e) for the purposes of this section, the net capital loss for the taxable year shall be the amount by which losses for such year from sales or exchanges of capital assets exceeds the sum of of the gains from such sales or exchanges and whichever of the following amounts is the lesser:

- (i) the corporation surtax net income (computed without regard to gains or losses from sales or exchanges of capital assets);
- or

(ii) losses from the sale or exchange of capital assets sold or exchanged to obtain funds to meet abnormal insurance losses and to provide for the payment of dividends and similar distributions to policyholders.

(c) *Rental Value of Real Estate*.—The deduction under subsection (b) (4) (C) or (b) (4) (D) of this section on account of any real estate owned and occupied in whole or in part by a mutual insurance company other than life or marine, shall be limited to an amount which bears the same ratio to such deduction (computed without regard to this subsection) as the rental value of the space not so occupied bears to the rental value of the entire property.

(d) *Amortization of Premium and Accrual of Discount*.—The gross amount of income during the taxable year from interest, the deduction provided in subsection (b) (4) (A), and the credit allowed against net income in section 26 (a) shall each be decreased by the appropriate amortization of premium and increased by the appropriate accrual of discount attributable to the taxable year on bonds, notes, debentures or other evidences of indebtedness held by a mutual insurance company other than life or marine. Such amortization and accrual shall be determined (1) in accordance with the method regularly employed by such company, if such method is reasonable, and (2) in all other cases, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary.

(e) *Deduction of Foreign Corporations*.—In the case of a foreign corporation the deductions allowed in this section shall be allowed to the extent provided in Supplement I in the case of a foreign corporation engaged in trade or business within the United States.

(f) *Double Deductions*.—Nothing in this section shall be construed to permit the same item to be twice deducted.



(g) *Credits Under Section 26.*—For the purposes of this section, in computing normal tax net income and corporation surtax net income, the credits provided in section 26 shall be allowed in the manner and to the extent provided in sections 13 (a) and 15 (a).

(26 U. S. C. 1946 ed., Sec. 207.)

Revenue Act of 1942, c. 619, 56 Stat. 798:

SEC. 101. TAXABLE YEARS TO WHICH AMENDMENTS APPLICABLE.

Except as otherwise expressly provided, the amendments made by this title shall be applicable only with respect to taxable years beginning after December 31, 1941.

SEC. 158. FOREIGN TAX CREDIT.

\* \* \* \* \*

(d) *Limit on Credit in Case of Corporations.*—Section 131 (b) is amended to read as follows:

“(b) *Limit on Credit.*—The amount of the credit taken under this section shall be subject to each of the following limitations:

“(1) The amount of the credit in respect of the tax paid or accrued to any country shall not exceed the same proportion of the tax against which such credit is taken, which the taxpayer’s net income from sources within such country bears to his entire net income, in the case of a taxpayer other than a corporation, or to the sum of the normal-tax net income and the amount of the credit for adjusted excess profits net income provided in section 26 (e), in the case of a corporation, for the same taxable year;

\* \* \* \* \*

Revenue Act of 1943, c. 63, 58 Stat. 21:

SEC. 130. TECHNICAL AMENDMENTS RELATING TO  
FOREIGN TAX CREDIT.

\* \* \* \* \*

(c) *Taxable Years to Which Applicable.*—The amendment made by subsection (a) shall be effective for all taxable years beginning after December 31, 1941. The amendment made by subsection (b) shall be effective with respect to all taxable years beginning after December 31, 1939.

Treasury Regulations 111, promulgated under the Internal Revenue Code:

SEC. 29.131-2. MEANING OF TERMS.—The term “amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year” means taxes proper (no credit being given for amounts representing interest or penalties) paid or accrued during the taxable year on behalf of the taxpayer claiming credit. For the purposes of section 131 and section 23 (c) (1) the term “income, war-profits, and excess-profits taxes” includes a tax imposed by statute or decree by a foreign country or by a possession of the United States if (a) such country or possession has in force a general income tax law, (b) the taxpayer claiming the credit would, in the absence of a specific provision applicable to such taxpayer, be subject to such general income tax, and (c) such general income tax is not imposed upon the taxpayer thus subject to such substituted tax. For example, the A Corporation does business in the X country, which imposes an income tax upon substantially a net income base. The ascertainment of net income, though not the determination of gross income, from sources in X country is found administratively difficult. The X country, by decree, provides that corporations circumstanced as was the A Corporation would, in lieu of the income tax at the rate of 20 per cent otherwise payable, be subject to tax at

the rate of 10 per cent upon the amount of gross income from X country. In accordance with such decree, the A Corporation paid X country the sum of \$25,000 in 1943 with respect to its tax liability to the X country for the year 1942. Such amount, subject to the applicable limitations, is available as a credit to the A Corporation as foreign income, war-profits, or excess-profits taxes against the United States tax liability for the year 1942. \* \* \*

H. R. 7378, 77th Cong., 2d Sess. [Revenue Bill of 1942 as reported and as passed House]:

SEC. 147. MUTUAL INSURANCE COMPANIES OTHER THAN LIFE.

\* \* \* \* \*

(b) *Taxable Companies*.—Section 207 (relating to taxation of mutual insurance companies other than life) is amended to read as follows:

“SEC. 207. MUTUAL INSURANCE COMPANIES OTHER THAN LIFE.

“(a) *Imposition of Tax*.—There shall be levied, collected, and paid for each taxable year upon the net income of every mutual insurance company (other than a life insurance company) the corporation surtax net income of which is over \$50,000, a tax computed as follows :

“(1) *Normal Tax*.—A normal tax on the normal-tax net income, computed at the rates provided in section 13, or 48 per centum of the amount by which the normal-tax net income exceeds \$50,000, whichever is the lesser; plus

“(2) *Surtax*.—A surtax on the corporation surtax net income, computed at the rates provided in section 15 (b), or 42 per centum of the amount by which the corporation surtax net income exceeds \$50,000, whichever is lesser.

“(3) *Ledger Assets Over \$100,000 But Less Than \$150,000*.—If the mean of the ledger assets

held at the beginning and end of the taxable year is over \$100,000 but less than \$150,000, the tax under this subsection shall be an amount which bears the same proportion to the sum of the lesser amounts ascertained under paragraphs (1) and (2) as the excess over \$100,000 of such mean of the ledger assets bears to \$50,000.

“(4) *Normal-tax and Corporation Surtax Net Income of Foreign Mutual Insurance Companies Other Than Life.*—In the case of a foreign mutual insurance company (other than a life insurance company), the normal-tax net income shall be the net income from sources within the United States minus the credit provided in section 26 (a), the credit provided in section 26 (b), and the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26 (c), and the corporation surtax net income shall be the net income from sources within the United States minus the credit provided in section 26 (b) (computed by limiting such credit to 85 per centum of the net income reduced by the credit for income subject to the tax imposed by Subchapter E of Chapter 2 in lieu of 85 per centum of the adjusted net income so reduced), and minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26 (e).

“(5) *No United States Insurance Business.*—Foreign mutual insurance companies (other than a life insurance company) not carrying on an insurance business within the United States shall not be taxable under this section but shall be taxable as other foreign corporations.

“(b) *Definition of Income, Etc.*—In the case of an insurance company subject to the tax imposed by this section—

“(1) *Gross Income.*—‘Gross income’ means the sum of (A) investment income as defined in paragraph (2), (B) underwriting income as de-



fined in paragraph (4), and (C) all other items constituting gross income under section 22;

“(2) *Investment Income*.—‘Investment income’ means the gross amount of income during the taxable year from interest, dividends, rents, and gains from sales or exchanges of capital assets to the extent provided in section 117, less (A) losses from sales or exchanges of capital assets to the extent provided in section 117, (B) investment expenses, (C) real estate expenses, (D) depreciation, and (E) interest paid;

“(3) *Investment Expenses, Etc.*—As used in this section the terms ‘investment expenses’, ‘real estate expenses’, ‘depreciation’, and ‘interest paid’ shall have the same meaning, and shall be subject to the same limitations, as in section 201 (c) (7) (B), (C) and (D), section 201 (c) (6) (A), and section 201 (d) (relating to life insurance companies), but shall be computed as if the word ‘paid’ wherever it appears therein were ‘paid or accrued’;

“(4) *Underwriting Income*.—‘Underwriting income’ means net premiums received during the taxable year on insurance contracts plus any decrease during such year in any of the items specified in subparagraph (C) less:

“(A) Losses paid in excess of salvage and reinsurance recoverable;

“(B) Underwriting expenses and loss adjustment expenses paid or accrued;

“(C) The increase during the taxable year in any of the following items: (i) unearned premiums; (ii) unpaid losses; and (iii) surplus apportioned to policyholders;

“(D) Dividends and similar distributions paid to policyholders out of premium income and surplus apportioned to policyholders. Dividends and similar distributions paid to policyholders shall be considered to be paid out of

premium income and surplus apportioned to policyholders only to the extent they exceed the sum of the investment income of the taxable year available to pay dividends and similar distributions in that year plus the investment income of the preceding taxable years (if beginning after December 31, 1941) available to pay such dividends and similar distributions in such years but not so used;

“(5) *Net Premiums Received*.—‘Net premiums received during the taxable year on insurance contracts’ means gross premiums (including premium deposits and assessments) written or received on insurance contracts less return premiums and premiums paid for reinsurance. Amounts returned where the amount is not fixed in the insurance contract but depends upon the experience of the company or the discretion of the management shall not be included in return premiums but shall be treated as dividends to policyholders under paragraph (4) (D);

“(6) *Surplus Apportioned to Policyholders*.—

“(A) *In General*.—‘Surplus apportioned to policyholders’ means such portion of the surplus of the company as is held for distribution to policyholders before the expiration of five years after the termination of their policies in equitable proportion to the amount of the surplus contributed by each policyholder or group of policyholders and includes amounts set aside for the payment of dividends and similar distributions to policyholders. The amount of surplus apportioned to policyholders shall in no case be considered to exceed an amount which would leave unapportioned surplus equal to or less than the unapportioned surplus as of the beginning of the first taxable year which begins after December 31, 1941;

“(B) *Limitation on Amount Includible*.—For the purposes of subparagraph (A), no

amount shall be included in surplus apportioned to policyholders unless, under the provisions of the insurance contract, or by the by-laws of the company, the distribution of such amount is specifically required and the distribution is not at the discretion of the directors of the company. The fact that the distribution of an amount can be withheld in order to comply with requirements of State law, or may be subjected to lien or assessment to meet abnormal loss or decline in market value of assets, shall not prevent the inclusion of such amount in surplus apportioned to policyholders. In no case shall an amount held for more than five years from the termination of the policy be included in surplus apportioned to policyholders;

“(C) *Special Rule for Taxable Years Beginning After December 31, 1941, and Before January 1, 1945.*—For the purposes of subparagraph (A), for taxable years beginning after December 31, 1941, and before January 1, 1945, an amount shall be included in surplus apportioned to policyholders if includible under subparagraph (B) or if payable to policyholders under the established normal practice of the company;

“(7) *Investment Income Available To Pay Dividends And Similar Distributions.*—‘Investment income available to pay dividends and similar distributions’ means investment income for the taxable year (computed without regard to section 117 (d) and (e) less (A) an amount equal to 21 per centum of the interest on obligations with respect to which a credit is allowable under section 26 (a) (relating to interest on certain obligations of the United States), and (B) an amount equal to 45 per centum of so much of the investment income (computed with regard to section 117 (d) and (e)) as exceeds the sum of (i) the interest on obligations with respect to

which a credit is allowable under section 26 (a), plus (ii) the interest on obligations described in section 22 (b) (4), plus (iii) the credit provided in section 26 (b) (relating to dividends received on stock of domestic corporations);

“(8) *Net Income*.—‘Net income’ means the gross income as defined in paragraph (1) of this subsection less the following deductions:

“(A) All deductions as provided in section 23 to the extent not otherwise allowed;

“(B) The amount of the net operating loss deduction provided in section 23 (s) except that in computing such deduction the terms ‘third preceding taxable year’, ‘second preceding taxable year’, and ‘first preceding taxable year’ as used in section 122 shall not include any taxable year beginning before January 1, 1942; and

“(C) The amount of interest which under section 22 (b) (4) is excluded for the taxable year from gross income.

“(c) *Deductions of Foreign Corporations*.—In the case of a foreign corporation the deductions allowed in this section shall be allowed to the extent provided in Supplement I in the case of a foreign corporation engaged in trade or business within the United States.

“(d) *Double Deductions*.—Nothing in this section shall be construed to permit the same item to be twice deducted.”

(c) *Cross Reference*.—For stamp tax on policies written by foreign insurers, see section 502 of this Act.



**In The United States Court of Appeals**  
**For the Ninth Circuit**

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NORTHWESTERN MUTUAL FIRE ASSOCIATION,  
*Appellant,*

vs.

COMMISSIONER OF INTERNAL REVENUE,  
*Appellee.*

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UPON APPEAL FROM THE TAX COURT OF THE  
UNITED STATES

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**REPLY BRIEF OF APPELLANT**

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JO DUDLEY COOK,  
FREDERICK J. ORTH,

*Of Counsel:*

*Attorneys for Appellant.*

RODE, COOK & WATKINS,  
217 Pine Street,  
Seattle 1, Washington.

JAN 27 1950



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JO DUDLEY COOK,  
FREDERICK J. ORTH,

*Of Counsel:* *Attorneys for Appellant.*

RODE, COOK & WATKINS,  
217 Pine Street,  
Seattle 1, Washington.





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**In The United States Court of Appeals**  
**For the Ninth Circuit**

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NORTHWESTERN MUTUAL FIRE ASSOCIA-  
TION,

*Appellant,*

vs.

COMMISSIONER OF INTERNAL REVENUE,

*Appellee.*

**No. 12338**

---

UPON APPEAL FROM THE TAX COURT OF THE  
UNITED STATES

---

**REPLY BRIEF OF APPELLANT**

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**A. MUTUALS NOT TAXED IN CANADA ON  
INVESTMENT INCOME**

Referring to Canada, appellee states (p. 7): "It just did not impose an income tax upon the investment income of mutual insurance companies, or upon any other income of such companies in 1942 and 1943 though it did later in 1946." That is not true. In 1946 Canada did not impose a tax upon the investment income of appellant. Though the Income War Tax Act was amended in 1946 the tax on mutuals such as appellant was not imposed until 1947. Then it was NOT imposed upon their investment income, but upon their net income excluding their investment income. Arguendo, if the "gross amount of income tax" imposed upon appellant under the Internal Revenue Code is "an income tax" then Canada did impose "an income tax" on "other income" of appellant, namely, on its "net premium income."

## B. APPELLANT'S U. S. TAX BASE WAS GROSS INCOME

In 1942 and 1943 appellant *was not* subject, under Section 207 I.R.C., to a federal income tax *imposed upon its entire investment income* derived both from sources in the United States and Canada. That statement is misleading. Appellant was "*subject to*" a federal income tax "*imposed upon*" its "*gross amount of income*" from sources in the United States and Canada under Section 207 (a) (2) I.R.C. (Tr. 18, 19, 56, 57). Its "*gross amount of income*" *included* its "*entire investment income*," but its "*investment income*" was a negligible factor. As pointed out in appellant's brief (page 37) 97% of appellant's gross amount of income consisted of "net premiums"—not more than 3% consisted of "investment income."

It is not true that "a normal-tax" of 30% was imposed upon the company's "normal-tax net income." *If the Internal Revenue Code had* imposed a tax on such basis its normal tax would have been 24% (*not 30%*) upon its "normal-tax net income" and a surtax of 14% (*not 20%*) upon its surtax net income. But such tax was not imposed upon appellant. During those years Section 207 (a) (2) imposed upon appellant a tax of 1% on its "*gross amount of income*" (Tr. 18, 19, 56, 57).

Appellee states that Section 207 (a) (2) imposes a tax of 1% "*upon the 'gross amount of income' exceeding \$75000 \* \* \*.*" That is not true! Under that section if the gross amount of taxpayers' income exceeds \$75,000 the tax of 1% is imposed upon its entire

“gross amount of income,” not, as appellee states upon the amount in excess of \$75,000.

### C. NO CASE HOLDS CANADIAN TAX A PRIVILEGE TAX

Referring to the Canadian Special War Revenue Tax appellee states: “This tax has been held to be a business privilege or franchise tax rather than an income tax \* \* \*.” The cases cited *do not* so hold! In the case of *Continental Insurance Co. v. Commissioner* (1939) 40 B.T.A. 540, quoted by the Tax Court in this case, the Board of Tax Appeals *held* that the Canadian Special War Revenue tax *was not* an “income tax” within the meaning of Section 131 (a) (1) of the Revenue Act of 1934. In its decision it stated: “It was *more like* an excise tax upon the privilege of doing business *than like* an income tax.” That is not a holding that it *was* a business privilege tax, and in any event is dicta. The holding of the Federal District Court in the case of *St. Paul Fire and Marine Insurance Co. v. Reynolds* (1942) 44 F. Supp. 863, 865, was to the same effect: “The premiums received were not income within the meaning of that term as used in Section 131 (a) (1) of the Revenue Acts (1933, 1934, 1935 and 1936) and the premium tax was not an income tax.” By way of dicta the federal court also observes that the Canadian tax is *more like* an excise tax than an income tax (based on profits) but it does not specifically so hold. In the case of *Helvering v. Queen Ins. Co.*, 115 F.2d 341, the taxpayer conceded that the Canadian Special War Revenue Tax *was not* “an income tax”

## F. CONGRESS INTENDED TO ALLOW CREDIT FOR TAX ON GROSS INCOME

Appellant agrees that the limitation feature of Section 131(b)(1) continues to apply to limit the amount of taxpayers' foreign tax credit as therein provided (See Appellant's Brief, Section G, pp. 77-86). Appellant does not agree (page 16) that “\* \* \* to carry out the Congressional intent, what we must look for is a Canadian tax based upon investment income, however measured \* \* \*.”

Appellees goes ahead to say “\* \* \* for example, as a tax upon gross investment income, or a tax upon the doing of an investment business, or a tax upon the holding of investments measured by their value \* \* \*.” If, to qualify as a credit under 131(h), Congress intended that the foreign tax had to be based upon “investment income” why was Section 131(h) added to the Internal Revenue Code? A tax based on investment income could qualify for a tax credit prior to 1942 under Section 131(a)(1) of prior revenue laws. Appellee disregards the facts. The taxpayer in this case is engaged in the insurance business (Tr. 24, 50), not in the investment business. Its investment income was a negligible factor in its taxable income under U.S. law (Appellant's Opening Brief, Appendix No. XI, p. A-13). The basis of its tax in this country was its “gross amount of income” (Tr. 18, 19, 56, 57, Appellant's Opening Brief, Appendix No. XI, p. A-13) *not* its investment income. The facts conclusively indicate that Congress intended Section 131(h) to permit a foreign tax credit where the foreign tax was measured by “gross income, gross sales or



number of units produced within the country \* \* \*” (Tr. 39). The standard suggested by appellee is contrary to the expressed intent of Congress.

#### **G. CONGRESS DID NOT INTEND ADMINISTRATIVE DIFFICULTIES TO BE A CONDITION PRECEDENT TO GRANT OF CREDIT**

Appellant’s reference to Treasury Regulation 103 was *not* inadvertent! It was intentional. Appellant’s reference (Appendix No. IX p. A 10) was to Treasury Regulation 103 as amended by T. D. 5226, 1943-4-71350 approved February 10, 1943. Treasury Regulation 111, Sec. 29, 131-2, is a comparable regulation issued in 1944. From it appellee argues that “the administrative difficulties a foreign country might have in determining net income” is a *sine qua non* to the granting of a foreign tax credit under 131 (h).

It is not an essential prerequisite according to the expressed intent of Congress (Tr. 39). The Senate Finance Committee stated in part: “Thus *if* \* \* \* for reasons growing out of the administrative difficulties of determining net income \* \* \*.” The words *are not*, as contended by appellee, *definitive* of the conditions under which the credit can be granted, but are purely *illustrative* as their context clearly shows.

#### **H. IN LIEU OF TAX MUST BE AN EXCISE TAX**

Appellees’ reference (page 18) to “the grant of credit on account of a *foreign excise* tax levied on mutual insurance companies” is inapt. By definition an “excise tax” is “any duty, toll or tax.” Webster’s New International Dictionary (unabridged).

In the modern sense it has been repeatedly held to be "any tax not falling within the classification of a poll or property tax." *Diefendorf v. Gallet* (1932) (Idaho) 10 P.(2d) 307, 312; 51 Am. Jur. 61, §33, and cases cited therein. Any tax imposed by a foreign country in lieu of an income tax would necessarily be an excise tax by definition, unless it was a poll or property tax.

**I. SECTION 207<sup>(a)</sup>(2) I.R.C. DOES NOT IMPOSE AN EXCESS TAX**

Appellee's statement (pages 18 and 19) that the so-called alternative "special tax" imposed upon appellant under Section 207 (a) (2) imposed only an "excess tax" over and above the amount of tax imposed under Section 207 (a) (1) is a gross misstatement of the law. (See Appellant's Opening Brief Appendix No. II p. A 3.) The law states in part: "There shall be levied, collected and paid \* \* \* upon the income of every mutual insurance company \* \* \* a tax computed under paragraph (1) OR paragraph (2) *which-ever is the greater* \* \* \*" (Emphasis supplied). It is not an excess tax. Neither is it an alternative tax. The provision is too plain to require further elaboration.

Appellee argues that the "so-called excess" was deliberately disregarded by Congress in fixing the limitation of credit under Section 131 (b). Appellant agrees! Congress examined the provisions of Section 131 (b) in 1942, found them adequate and therefore did not change them.

## **J. APPELLANT'S NET PREMIUMS TAXED IN BOTH CANADA AND U. S.**

Appellee makes some pertinent observations and admissions (page 19) that will bear emphasizing. Section 207(a) (2) I.R.C. and Section 131 (h) I.R.C. were both enacted in 1942. Appellee admits that if the House amendment to 207 had passed, appellant would be entitled to claim the credit under Section 131 (h). Why this admission? It is because the House amendment tax included "net premiums" which were similarly defined in the Canadian Act. Section 207 (a) (2) I.R.C. also includes "net premiums" which, in Section 207 (b) (2) are similarly defined in the Canadian Act. They are the same "net premiums" on which appellant was subject to tax in 1942 and 1943 in both Canada and the United States. Appellee gives no convincing argument why that is not the "double taxation" against which Congress intended to grant relief when it expanded Section 131 I.R.C. by the addition of subsection (h).

## **K. THE COMMISSIONER'S TEST IGNORES THE 1942 AMENDMENT ADDING SUBSECTION (h) TO 131 I.R.C.**

Appellee asserts (page 20) "\* \* \* nowhere is there the slightest indication that Congress intended by Section 131 (h) to permit the inclusion in the credit base of anything but 'normal-tax net income,' or to allow the credit to be taken on account of a foreign tax which was not levied in respect of such base." That fairly summarizes appellee's argument. If the foreign tax is not on "normal tax net income" it can-

not qualify as a foreign tax credit. That was the Commissioner's argument prior to the 1942 amendment of Section 131 I.R.C. That is his argument now after the addition in 1942 of subsection (h) to Section 131 I.R.C. Appellee does not dispute appellant's argument that Section 131 was originally enacted to mitigate the evil of double taxation. Appellee does not deny that subsection (h) was added to broaden the basis for allowing foreign tax credits so that that section might thereby carry out more effectively its salutary purpose. Prior to 1942 a foreign tax based upon "normal-tax net income" was allowed as a foreign tax credit under Section 131 (a) (1). If Congress did not intend to allow a foreign tax as a credit unless it was based upon "normal-tax net income," why did Congress bother to add subsection (h) to Section 131? The intent of Congress as expressed by the Senate Finance Committee which sired the amendment which added subsection (h) was to permit a foreign tax credit *even though* the foreign tax *was not* based on taxpayer's "normal-tax net income"—even though the foreign tax was based upon taxpayer's "gross income, gross sales or number of units produced in the country" (Tr. 39). Appelle's conclusion quoted above does not answer part III (b) of appellant's brief pp. 27-31.



## L. CREDITS ARE NOT THE SAME AS DEDUCTIONS AND EXEMPTIONS

The cases cited by appellee all deal with exemptions or deductions. Not one applies the rule quoted to a claim of credits against tax. There is a distinction:

“Deductions and exemptions are two separate and distinct things, having no connection. A deduction is the taking of the subtrahend from the minuend; it is a subtraction. Exemption is an immunity or privilege; it is a freedom from a charge or burden to which others are subject.”

*Florer v. Sheridan* (1894, Ind.) 36 N.E. 365, 369.

The U. S. Supreme Court recognized and emphasized the distinction between “credits” and “deductions” in the case of *Burnet v. Chicago Portrait Co.* (1932) 285 U.S. 1, 15, 76 L. ed. 587, 10 A.F.T.R. 800, where in discussing the change in the U. S. Internal Revenue Code from allowing foreign taxes as a “deduction” to allowing them as a “credit” Chief Justice Hughes stated:

“*The distinction made with respect to income taxes paid to the States of the Union, and their political subdivisions, between deductions from gross income and credits against taxes, simply reflects the economic policy adopted in making allowances for taxes paid within the borders of Continental United States and the organized territories. In relation to income taxes paid outside these borders the provision as to credits was enacted to give greater and not less relief \* \* \**” (Emphasis supplied)

Since appellant is not claiming an “exemption” or a

“deduction” but a “credit” appellee’s authorities are not in point. In any event appellant has cited the applicable statutory provision which entitles it to the credit claimed, and has clearly shown its right to come within the terms of that section.

### **M. AN OBJECTIVE TEST FOR RELIEF UNDER SECTION 131(h) I.R.C.**

Appellee fails to answer with authorities the main points of appellant’s argument. No constructive suggestions are made for an objective test, to be applied, to determine the allowability of a foreign tax credit under Section 131(h)IRC. Appellant, therefore, suggests the following objective test:

*Is the tax one imposed by a foreign country on a basis other than net income where the taxpayer (exempt from payment of a net income tax) is subject to a tax measured substantially by gross income, gross sales or number of units produced within such country?*

The proposed test embodies all of the essential prerequisites set forth in the law, and the report of the Senate Finance Committee which amended the law. Its application will carry out the intent of Congress in enacting the amendment.

## N. CONCLUSION

If applied in this case appellant is clearly entitled to the credits claimed. Indeed in appellee's brief there is not one argument, supported by authority, that answers or in any way refutes the arguments in appellant's opening brief. For the reasons set forth therein appellant is entitled to the foreign tax credits claimed. Appellant is entitled to judgment reversing the decision of the Tax Court and awarding it foreign tax credit refunds claimed.

Respectfully submitted,

JO DUDLEY COOK,

FREDERICK J. ORTH,

*Of Counsel:*

*Attorneys for Appellant.*

RODE, COOK & WATKINS,

217 Pine Street,

Seattle 1, Washington.





IN THE  
**United States**  
**Court of Appeals**  
FOR THE NINTH CIRCUIT

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JOHN C. EDWARDS, JR.,

*Petitioner-Appellant,*

vs.

P. J. SQUIER, Warden, United States

Penitentiary, McNeil Island, Washington,

*Respondent-Appellee.*

---

ON APPEAL FROM THE DISTRICT COURT OF THE UNITED  
STATES FOR THE WESTERN DISTRICT OF WASHINGTON,  
SOUTHERN DIVISION.

---

HONORABLE CHARLES H. LEAVY, *Judge*

---

**BRIEF OF APPELLEE**

---

J. CHARLES DENNIS,  
*United States Attorney*

GUY A. B. DOVELL,  
*Assistant United States Attorney*  
*Attorneys for Appellee*

OFFICE AND POST OFFICE ADDRESS:  
324 FEDERAL BUILDING  
TACOMA 2, WASHINGTON

---



No. 12339

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IN THE  
**United States**  
**Court of Appeals**  
FOR THE NINTH CIRCUIT

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JOHN C. EDWARDS, JR.,

*Petitioner-Appellant,*

VS.

P. J. SQUIER, Warden, United States

Penitentiary, McNeil Island, Washington,

*Respondent-Appellee.*

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ON APPEAL FROM THE DISTRICT COURT OF THE UNITED  
STATES FOR THE WESTERN DISTRICT OF WASHINGTON,  
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---

J. CHARLES DENNIS,  
*United States Attorney*

GUY A. B. DOVELL,  
*Assistant United States Attorney*  
*Attorneys for Appellee*

OFFICE AND POST OFFICE ADDRESS:  
324 FEDERAL BUILDING  
TACOMA 2, WASHINGTON

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IN THE  
**United States**  
**Court of Appeals**  
FOR THE NINTH CIRCUIT

---

JOHN C. EDWARDS, JR.,  
*Petitioner-Appellant,*  
vs.

P. J. SQUIER, Warden, United States  
Penitentiary, McNeil Island, Washington,  
*Respondent-Appellee.*

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ON APPEAL FROM THE DISTRICT COURT OF THE UNITED  
STATES FOR THE WESTERN DISTRICT OF WASHINGTON,  
SOUTHERN DIVISION.

---

HONORABLE CHARLES H. LEAVY, *Judge*

---

**BRIEF OF APPELLEE**

---

**STATEMENT OF PLEADINGS AND FACTS**

Appellant on May 25, 1949 lodged with the Clerk of the United States District Court for the Western District of Washington, Southern Division, his petition for a writ of habeas corpus (Tr. 3 - 8), and therewith filed an affidavit in forma pauperis (Tr. 1 - 2),

whereupon the District Court on June 2, 1949, directed the application to be filed and ordered appellee to show cause in the matter by filing a return to the petition and attaching thereto a certified copy of the information, plea and judgment as material to the issue, the appellant having failed so to do in connection with his petition. (Tr. 9 - 10).

To the order to show cause, appellee filed a return and attached thereto the documents as theretofore required. (Tr. 11 - 17).

Thereafter on June 24, 1949, pursuant to notice of motion served on appellant on June 21, 1949 (Tr. 20), the appellant filed his traverse to the return made by appellee. (Tr. 18 - 19).

On August 1, 1949, upon motion to dismiss, noted and served by appellee, (Tr. 21 - 23), the court made and entered an order denying appellant's petition for writ of habeas corpus, and dismissing the action. (Tr. 24 - 25). From that final order, the appellant has been permitted to appeal in forma pauperis. (Tr. 26 - 31).

The facts material to a determination of appellant's right to relief, as disclosed in the record, may be summarized as follows:

On March 26, 1947, an Information containing



two counts was filed against appellant in the Northern Division of the United States District Court for the Northern District of California, which information in the first count charged the defendant with transporting a stolen motor vehicle from Houston, Texas, to Sacramento, California, on or about March 16, 1947, and in the second count charged the defendant with transporting on or about March 16, 1947, in interstate commerce securities of the approximate value of \$22,625.00, which on or about February 22, 1947, at Houston, Texas, had been stolen, and with knowing the same to have been stolen. (Tr. 14).

Thereafter, on April 16, 1947, the appellant having waived his right to assistance of counsel, and entered a plea of guilty thereto, he was adjudged guilty and convicted, and was sentenced to two years on the first count and six years on the second count, said periods of imprisonment so imposed to commence and run consecutively. (Tr. 15).

### QUESTIONS PRESENTED

1. May not offenses under the National Motor Vehicle Theft Act and the National Stolen Property Act, be charged respectively in separate counts of the same information?

2. Can a person sentenced under such an in-

formation be released on habeas corpus on the ground, if it be so determined, that distinct offenses were improperly joined?

## ARGUMENT AND AUTHORITIES

The pertinent portions of the statutes defining the offenses charged in the information, in the order of the counts, are as follows:

### *National Motor Vehicle Theft Act*

“ \* \* \* Whoever shall transport or cause to be transported in interstate commerce a motor vehicle or aircraft, knowing the same to have been stolen, shall be punished by a fine of not more than \$5,000 or by imprisonment of not more than five years, or both.”

Title 18, U.S.C.A., Section 408.

### *National Stolen Property Act*

“Whoever shall transport or cause to be transported in interstate or foreign commerce any goods, wares or merchandise, securities, or money, of the value of \$5,000 or more theretofore stolen, \* \* \* knowing the same to have been so stolen, \* \* \* shall be punished by a fine of not more than \$10,000 or by imprisonment for not more than ten years, or both: \* \* \*”

Title 18, U.S.C.A., Section 415.

The pertinent portion of the Rule covering joinder of offenses, effective May 21, 1946, and applicable in this instance, is as follows:

“Two or more offenses may be charged in the

same indictment or information in a separate count for each offense if the offense charged, whether felonies or misdemeanors, or both are of the same or similar character or are based on the same act or transaction or on two or more acts or transactions connected together or constituting parts of a common scheme or plan." Rule 8, par. (a), Federal Rules of Criminal Procedure, following Sec. 687, Title 18, U.S.C.A.

1. *Offenses charged in information may be properly joined.*

It is true that Section 419, Title 18, U.S.C.A. provided:

"Nothing in Sections 413 - 418 of this title shall be construed to repeal, modify, or amend any part of Section 408 of this title, cited as the 'National Motor Vehicle Theft Act'."

However, appellee does not agree that it was for the reasons assigned by appellant, to create distinct offenses, but, more likely, it was to overcome the prospective contentions that Section 415, being the later enactment, had replaced Section 408, and for such reason only the transportation of cars of \$5,000.00 value or higher was intended to be prohibited.

Appellant finds support for his contentions in the case of *U. S. ex rel Valotta v. Ashe*, 2 Fed. (2d) 735, a habeas corpus matter decided by the District Court of the Western District of Pennsylvania, November 17, 1924.

While appellee does not desire to elaborate upon the advancement in criminal procedure, as disclosed by the above cited Rule 8, since the year of 1924 and the law then in effect, it should be pointed out that the Valotta case was concerned with actual trial before a jury for two murders, and it was held, in the language of headnote 5:

“The trial of one for two felonies at the same time and before the same jury was a denial of due process of law, notwithstanding accused made no objection, and judgments of conviction were null and void.”

Two indictments charging murder were found against Valotta and a single trial was had thereon.

In the instant case, the appellant plead guilty to an information containing two counts. Appellant, however, has failed to explain how being charged with two offenses was prejudicial in the face of his plea of guilty, so that it could be said that there was a denial of due process.

Again in the case of *McElroy v. United States*, 164 U.S. 76, a matter in error to the Circuit Court of the United States for the Western District of Arkansas to review a judgment of conviction of the plaintiffs in error, on the trial of several indictments consolidated, which were for distinct offenses at different times, the Supreme Court reversed the lower court



and remanded the cause with directions for a new trial, and for further proceedings.

However, it should be observed that in that case the Supreme Court discussed a similar situation as presented in the instant case which involved the facts in *Pointer v. United States*, 151 U.S. 396, where, as here, the unity of time, place and action rendered the proof the same as to both, and made the two alleged murders in that case substantially parts of the same transaction so much so that it was apparent to the Supreme Court that the substantial rights of the accused were not prejudiced by the action of the trial court, and the Supreme Court declined to reverse on the grounds of error therein. This part of the decision in the McElroy case apparently was not considered by the Pennsylvania court in arriving at its decision in the Valotta case, *supra*.

Appellant in his efforts to establish misjoinder seeks to separate the transaction involved in the second count from its relationship with the first count. If appellant had entertained any doubt as to the relationship of the two counts, he would at the proper time have been entitled to ask for a bill of particulars.

See *Myles v. United States*, 170 F. (2d) 443.

But appellant having plead guilty to transportation of securities of a value of \$5,000.00 in interstate

commerce on the day mentioned also in the first count, his plea admitted all these material facts, and the same is not open to review in these proceedings.

See *Caldwell v. Hunter*, 163 F. (2d) 181;  
*Tilghman v. Hunter*, 167 F. (2d) 661;  
*Dalton v. Hunter*, 174, F. (2d) 633;  
*Hawkins v. Sanford*, 53 F. Supp. 988.

Whether tested by Rule 8 or the decisions of the Supreme Court, there appears to be no misjoinder of counts in the instant case.

See *Pointer v. United States*, supra;  
*Kotteakos v. United States*, 328 U.S. 750,  
 772 - 775.

2. Distinct and separate offenses improperly joined in the same information do not render sentences thereon null and void and entitle the person so sentenced to release on habeas corpus.

Certainly, if the offenses were not separate and distinct, but constituted a single offense, the appellant would be entitled to release on habeas corpus.

*Morgan v. Devine*, 237 U.S. 632.

On the other hand, appellant seeks release on the grounds as stated in the "Summary" to his brief:

"As the bill of information shows, the appellant has been subjected to a practice which has been

ruled by the Supreme Court as illegal, inasmuch as there were two separate and distinct charges entered on one bill of information, and two separate and distinct sentences given to run consecutively."

While there may be contentions as to what constitutes separate and distinct offenses, the principle that a person sentenced on an information as above described cannot be released on habeas corpus on the ground that distinct offenses were improperly joined, still stands uncontested.

Ex parte *Peters*, 12 Fed. 461.

And it has been held:

"That an indictment charged more than one offense, in violation of the laws of the territory where petitioner was convicted, was a mere error of procedure, which did not divest the trial court of its power to render judgment, and was therefore, not ground for petitioner's discharge on habeas corpus."

*Connella v. Haskell*, 158 Fed. 285, 288.

## CONCLUSION

For the foregoing reasons, it must be contended that the decision below should be affirmed.

Respectfully submitted,

J. CHARLES DENNIS,  
*United States Attorney*

GUY A. B. DOVELL,  
*Assistant United States Attorney  
Attorneys for Appellee.*



No. 12340

---

United States  
Court of Appeals  
For the Ninth Circuit.

---

BOOTH-KELLEY LUMBER COMPANY, a Corporation,

Appellant,

vs.

SOUTHERN PACIFIC COMPANY, a Corporation,

Appellee,

and

SOUTHERN PACIFIC COMPANY, a Corporation,

Appellant,

vs.

BOOTH-KELLEY LUMBER COMPANY, a Corporation,

Appellee.

---

Transcript of Record

---

Appeals from the United States District Court,  
for the District of Oregon

FILED  
DEC 21 1949



No. 12340

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United States  
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BOOTH-KELLEY LUMBER COMPANY, a Corporation,

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Transcript of Record

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Appeals from the United States District Court,  
for the District of Oregon





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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS  
OF RECORD

VEAZIE, POWERS & VEAZIE, and

JAMES ARTHUR POWERS,

611 Corbett Building,

Portland, Oregon,

For Appellant.

KOERNER, YOUNG, SWETT & McCOLLOCH,

JAMES C. DEZENDORF,

ALFRED H. CORBETT,

800 Pacific Building,

Portland, Oregon,

For Appellee.

In The District Court of The United States  
For The District of Oregon

Civil No. 3989

SOUTHERN PACIFIC COMPANY, a corporation,  
Plaintiff,

Plaintiff,

vs.

THE BOOTH-KELLY LUMBER COMPANY,  
Defendant.

### COMPLAINT

Comes now plaintiff and for cause of action against defendant alleges:

#### I.

Plaintiff is a Delaware corporation engaged in the business of a common carrier by railroad in interstate and intrastate commerce in Oregon. Defendant is an Oregon corporation. The amount in controversy exclusive of interest and costs, exceeds the sum of \$3000.00.

#### II.

On or about June 30, 1941, Southern Pacific Company entered into an Industrial Track Agreement with defendant, The Booth-Kelly Lumber Company, covering the maintenance and operation of industrial track facilities serving defendant's Springfield mill, a copy of which agreement is attached hereto, marked Exhibit "A", and by this reference made a part hereof.



## III.

In this contract, defendant agreed that, without the prior written consent of Southern Pacific Company, it would not maintain any structure or obstruction of any character upon or over the premises of Southern Pacific Company.

## IV.

The agreement also contained the promise of Defendant to indemnify and hold Southern Pacific Company harmless for loss, damage, injury or death for any act or omission of Defendant, its employees or agents, to the person or property of the parties to the agreement and their employees while on or about said track.

## V.

On February 8, 1945, Mack D. Powers was employed as brakeman for Southern Pacific Company. He was engaged as part of the crew on one of Southern Pacific Company's trains which was switching over the track covered by said agreement. While so engaged, and while riding on the caboose, Mack D. Powers was injured by being caught between the side of the caboose and a wood cart which had been placed and maintained on the premises of Southern Pacific Company by defendant, its employees or agents, in a position approximately 42 inches from the outside of the outside rail.

## VI.

Said employee brought action against Southern Pacific Company for damages for his injuries under

the provisions of the Federal Employer's Liability Act. The complaint alleged breach of Southern Pacific Company's statutory duty of using ordinary care to provide said Mack D. Powers with a reasonably safe place in which to work in that, first, it caused and permitted the wood cart to remain on the track, and second, it failed to warn him of the presence of the wood cart and the resultant insufficient clearance.

## VII.

At trial the allegation that Southern Pacific Company caused and permitted the wood cart to remain on the track was removed from the jury's consideration because of lack of evidence. A verdict was returned for said Mack D. Powers upon the second count and judgment was duly entered.

## VIII.

Subsequently plaintiff was obliged to pay, and did pay, the sum of \$44,699.46 in satisfaction of said judgment. In addition to said amount plaintiff was obligated to pay, and has paid \$1869.53 in necessary costs and attorney's fees in defending said action.

## IX.

Shortly following the filing of said action against it, plaintiff gave timely Notice and made timely Demand and Tender of Defense upon defendant, a copy of which Notice, Demand and Tender is attached hereto, marked Exhibit "B", and by reference made a part hereof. Defendant denied any

liability and refused to assume the defense of said action. Subsequent to the rendering of the judgment plaintiff made demand upon defendant for the payment of \$44,699.46 judgment costs plus \$1869.53 additional costs of defending the action, which sums defendant fails and refuses to pay.

Wherefore, plaintiff prays:

1. For judgment against defendant for damages for breach of said contract in the sum of \$46,568.99,  
or

2. For judgment requiring defendant to indemnify and reimburse plaintiff in the sum of \$46,568.99, and for its costs and disbursements incurred herein.

KOERNER, YOUNG, SWETT  
& McCOLLOCH,  
/s/ JAMES C. DEZENDORF,  
/s/ ALFRED H. CORBETT,  
Attorneys for Plaintiff.

---

EXHIBIT "A"

(Copy)

Southern Pacific Company—Pacific Lines  
Industrial Track Agreement

This Agreement, made this 30th day of June, 1941, by and between Southern Pacific Company, a corporation hereinafter called "Railroad," and Booth-Kelly Lumber Company, a corporation, hereinafter called "Industry",

## Exhibit "A"—(Continued)

## Recitals:

Industry has requested Railroad to maintain and operate industrial track facilities, hereinafter called "Track," described as follows: Spur track, approximately 2,257 feet in length, at or near Springfield Station, County of Lane, State of Oregon. The location of said Track is shown by dashed red line and by solid red line on the map hereto attached and made a part hereof.

## Agreement:

Now, Therefore, in consideration of the agreements hereinafter contained to be kept and performed by the parties hereto, it is mutually agreed that the said Track shall be maintained and operated under the following terms, covenants and conditions:

1. The term "Track" as used herein shall designate the plural number if there is more than one track, and shall include all appurtenances thereof, consisting of rail and fastenings, switches and frogs complete, bumpers, ties, ballast, roadbed, embankment, trestles, culverts and any other structures and things necessary for the support of and entering into the construction of said Track, and if said Track, or any portion thereof, is located in a thoroughfare, said term "Track" shall include pavements, culverts, drainage facilities and all other work required by lawful authority in connection with the construction, renewal, maintenance and operation of said Track.



## Exhibit "A"—(Continued)

2. Industry will secure and furnish at its expense all necessary franchises and permits and right of way beyond the premises of Railroad for the construction and maintenance of said Track and for the operation of locomotives, motors, trains and cars thereon and thereover, except in the event that any State or Municipal body from which it is necessary to obtain franchises or permits shall require that the application be made by Railroad, in which event application therefor shall be made by Railroad. In the event Railroad applies for and secures said franchises or permits, Industry expressly agrees to pay any and all expenses incurred by Railroad in obtaining said franchises or permits, and all sums which may be expended at any time or times by Railroad under the provisions of said franchises or permits.

3. All material in said Track furnished at the expense of Railroad and not paid for by Industry, whether in original construction or by way of replacements or repairs, shall be and remain the exclusive property of Railroad. In the event said Track is disconnected, or upon termination of this agreement, Railroad may recover from the land of the Industry all the material owned by Railroad, and Industry, if said Track or any portion thereof is located in a thoroughfare, will pay the cost of removing all material owned by Industry and restoring the thoroughfare in good condition, satisfactory to the proper lawful authority, and Industry, provided no default shall then exist as to any covenants

## Exhibit "A"—(Continued)

or or agreements to be kept and performed by Industry, may recover all material owned by Industry and located on land of Railroad; provided, however, Railroad, at its option, may perform at the sole cost and expense of Industry all work of dismantling, taking up and removing said material owned by Industry and placing the ground in its original condition. Notwithstanding anything to the contrary herein contained, Railroad shall have the right at any time to purchase at its then value any or all material in said Track owned by Industry and not located on land of Industry.

4. Railroad agrees to operate said Track and to serve Industry thereon, subject to any lawful charges that may be made by Railroad for such service; said Track shall be under control of Railroad and Railroad shall have the right to use the same when not to the detriment of the Industry.

5. Industry agrees that without the written consent of Railroad first had and obtained, no structure, material, pole, cable, wire, conduit, pipe, opening, excavation or obstruction of any character shall be erected, piled, made, stored or maintained upon or over the premises of Railroad, or beneath any track upon the premises of Railroad. In the event such written consent is given, Industry agrees to comply with the following minimum clearances:  
Item:

Structures, material, poles or other obstructions of any character, except as shown below:

Exhibit "A"—(Continued)

Clearance:

A minimum side clearance of six (6) feet measured horizontally from outside of nearest track rail.

Item:

Platforms in excess of four (4) feet in height measured vertically from top of nearest track rail:

Clearance:

A minimum side clearance of six (6) feet measured horizontally from outside of nearest track rail.

Item:

Platforms four (4) feet or less in height measured vertically from top of nearest track rail:

Clearance:

A minimum side clearance of four (4) feet nine (9) inches measured horizontally from outside of nearest track rail.

Item:

Structures over or across any track and for a distance of at least six (6) feet from the outside of the rails thereof:

Clearance:

A minimum overhead clearance of twenty-two (22) feet measured vertically above tops of rails.

Item:

Wires over or across any track and for a distance of at least six (6) feet from the outside of the rails thereof:

## Exhibit "A"—(Continued)

## Clearance:

A minimum overhead clearance of twenty-five (25) feet measured vertically above tops of rails.

The above side clearances are for straight track. Along and adjacent to and for one car length beyond all portions of curved track, a side clearance of one foot greater than the minimum side clearance prescribed for straight track shall be maintained.

If, however, by statute or order of competent public authority greater clearances than those specified in this section shall be required, Industry expressly agrees to strictly comply with such statute or order.

All doors, windows or gates shall be of the sliding type, or shall open toward the inside of the building or enclosure when such building or enclosure is so located that said doors, windows or gates if opening outward would when opened, impair the clearances in this section provided.

Industry also agrees to comply with all the provisions of this section with respect to clearances on the property beyond the premises of Railroad, and that no pipe, conduit, structure, opening or excavation of any kind whatsoever, shall be made or placed beneath any track, or within ten (10) feet thereof, beyond the premises of Railroad without first giving Railroad written notice thereof.

6. Industry agrees that under no circumstances shall any gunpowder, dynamite or other explosive



## Exhibit "A"—(Continued)

material be piled or stored by Industry or others upon the premises of Railroad.

In the event said Track is used by Industry for the loading or unloading of oils, gasoline, other inflammable liquids or liquified petroleum gases, Industry agrees to observe Railroad's Rules governing the location of new loading and new unloading points for Casinghead gasoline, Refinery gasoline, Naphtha, Inflammable Liquids or Liquified petroleum gases, and Practice Rules for the protection of oil sidings or spurs where inflammable Liquids or Liquified petroleum gases are loaded or unloaded from danger due to stray electrical currents and static electricity. A copy of said Rules will be furnished by Railroad to Industry upon request of Industry, and Industry agrees to be bound by and carry out each and every provision set forth in said Rules.

7. It is understood that the movement of railroad locomotives involves some risk of fire, and Industry assumes all responsibility for and agrees to indemnify Railroad against loss or damage to property of Industry or to property upon its premises, regardless of Railroad's negligence, arising from fire caused by locomotives operated by Railroad on said Track, or in its vicinity, for the purpose of serving said Industry, except to the premises of Railroad and to rolling stock belonging to Railroad or to others, and to shipments in the course of transportation.

Industry also agrees to indemnify and hold harm-

## Exhibit "A"—(Continued)

less Railroad for loss, damage, injury or death from any act or omission of Industry, its employes or agents, to the person or property of the parties hereto and their employes, and to the person or property of any other person or corporation, while on or about said Track; and if any claim or liability, other than from fire, shall arise from the joint or concurring negligence of both parties hereto, it shall be borne by them equally.

8. Railroad may rearrange or reconstruct the Track or modify the elevation thereof whenever necessary or desirable in connection with the improvement of its property or changes in its tracks at or near the location of said Track, provided that the Industry shall continue to have similar trackage, without additional cost to the Industry. In the event, however, that a rearrangement or reconstruction of the Track, or modification of the elevation thereof, is required by reason of or as a result of any law, ordinance or other public enactment or regulation, or by reason of the happening of any contingency over which the Railroad has no control, then the Industry shall bear the cost of such rearrangement, reconstruction or modification. Nothing in this section contained shall in any way affect the right of the Railroad to terminate this agreement under the conditions hereinafter set forth.

9. Railroad shall have the right to disconnect the said Track or refuse to operate over the same,

## Exhibit "A"—(Continued)

and in either case this agreement at the option of Railroad shall terminate, in the event that (a) Industry shall cease to do business on said Track in an active and substantial way for a continuous period of one (1) year, unless prevented from so doing by law, strikes or any causes beyond the control of the Industry; (b) Industry shall fail to observe and perform each and every of the covenants and promises herein contained which are by Industry to be observed and performed, or (c) Railroad is required or authorized by law, ordinance or police regulations, or orders of any lawfully constituted public authority having jurisdiction in the premises, to discontinue operation of said Track, or to change its tracks in such manner as to render it impracticable, in the judgment of Railroad, to continue to operate said Track.

10. This agreement is not to be construed as extending, altering, amending, modifying or forming a part of any instrument in writing between the parties hereto, or their predecessors or successors in interest, with respect to the use by Industry, or its successors in interest, of any premises of Railroad or its lessor.

11. It is understood and agreed that Sections 12 to 21, inclusive, hereof, on insert hereto attached, are hereby made parts of this agreement.

This agreement shall be binding upon the heirs, executors, administrators, successors and assigns of the parties hereto.

## Exhibit "A"—(Continued)

In Witness Whereof, the parties hereto have executed this agreement in duplicate the day and year first hereinabove written.

Recommended

J. W. CORBETT  
Superintendent  
SOUTHERN PACIFIC  
COMPANY

[Seal] By L. B. McDONALD  
General Manager

Attest:

ROY G. HILLEBRAND  
Asst. Secretary  
BOOTH-KELLY LUMBER  
COMPANY

[Seal]

By CHAS. G. BRIGGS  
President

Attest:

N. A. DUNBAR  
Secretary

Description Correct

H. A. HAMPTON

Form Approved:

A. E. STEWART  
Contract Attorneys

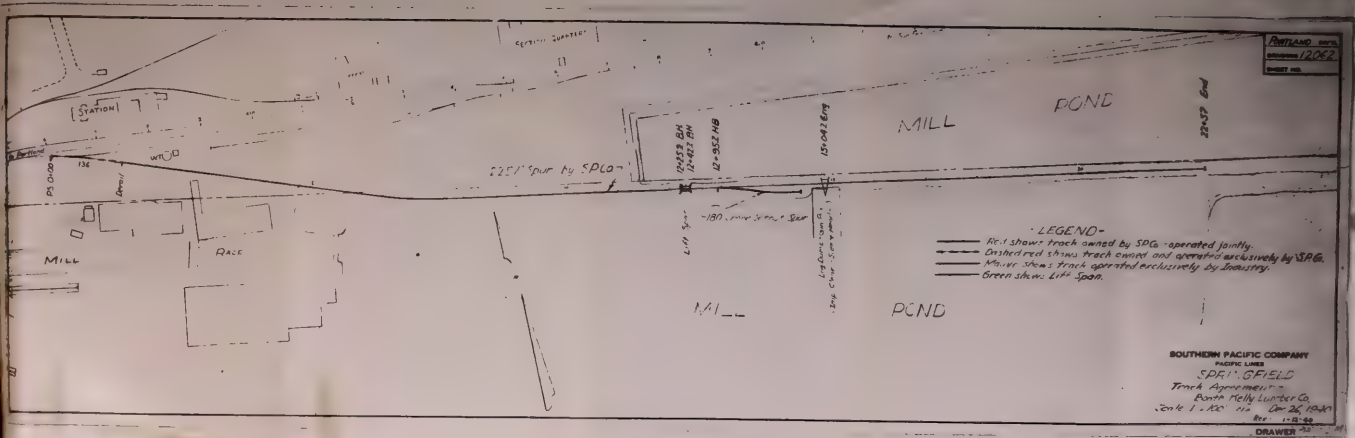
Witnessed By:

F. C. CRAWFORD  
EMMA N. DRAIN

Form of Execution Approved.

E. C. CROCKER







## Exhibit "A"—(Continued)

Copy

Insert

12. Under dates of January 4, 1909 and February 27, 1909 the parties hereto entered into certain agreements relating to the construction, maintenance and operation of industrial trackage at said Springfield, which trackage is now located as shown by dashed red line and by solid red line on said map and is hereinafter referred to as said "Track". In the construction of said Track Railroad paid for and furnished all metal required therein and Industry paid for the ties, grading, ballast and labor.

13. Railroad at its own expense shall maintain said Track, except that Industry, to the satisfaction of Railroad and at Industry's expense, shall maintain the subgrade therefor and shall continue to maintain a certain lift span trestle therein (as more specifically provided in that certain supplemental agreement between the parties hereto dated August 14, 1940), and any other trestles or structures supporting said Track.

14. The provisions of Section 5 of this agreement shall not apply to any clearances in violation thereof existing as of the date hereof, i.e., two (2) brow skids and an overhead unloading device; provided, however, that Industry shall release and discharge and agree to indemnify and save harmless Railroad from and against any and all loss, damage, injury, death, cost, expense and liability

## Exhibit "A"—(Continued)

of every kind and nature resulting directly or indirectly from the existence of said impaired clearances. It is expressly agreed that this agreement shall not be construed as authorizing Industry to maintain any impaired clearances along or over said Track except those specifically referred to above.

15. Notwithstanding the provisions of Section 4 hereof, Railroad shall not be required to place cars loaded with logs at any specified point on said Track for unloading, but all incoming cars loaded with logs shall be delivered by Railroad to Industry on the portion of said Track in the general vicinity of the track shown by mauve line on said map and marked "180' Crane Setout Spur." Industry agrees to accept delivery of said cars of logs at the point of delivery as defined in this Section 15, and such cars and their contents shall be considered in the custody of Industry from the time the same are placed by Railroad on said Track until switched therefrom by Railroad.

16. Industry shall have the right to move cars on the portion of said Track shown by solid red line by means of a cable attached to a traveling crane; also to move a traveling crane upon such portion of Track; provided, however, no car or crane shall be moved by Industry at such time or times as Railroad is operating or about to operate on said Track, or in such manner as to interfere with, delay or endanger switching operations of Railroad.



## Exhibit "A"—(Continued)

17. Industry agrees to return to Railroad all cars delivered to Industry by Railroad in as good condition as when received, ordinary wear and tear excepted. In the event any of said cars are not so returned by Industry to Railroad in as good condition as when delivered to Industry, ordinary wear and tear excepted, Railroad is hereby requested to make necessary repairs to said cars at the expense of Industry, which expense shall be paid to Railroad by Industry on demand, and should any of said cars delivered by Railroad to Industry be destroyed, or for any reason not returned to Railroad, Industry agrees to pay to Railroad the value of said cars, said value to be determined by Railroad; provided, however, Industry shall not be liable for any loss or destruction of or damage to cars caused by the negligence of Railroad, except as herein otherwise provided.

18. In addition to but not in qualification of the provisions of Sections 7 and 17 hereof, Industry hereby releases and discharges and agrees to indemnify and save harmless Railroad, its agents, successors and assigns, from all liability resulting directly or indirectly from the movement of cars and/or operations by Industry upon said Track.

19. The track shown by mauve line on said map is owned and shall be maintained by Industry, and Railroad shall not be obligated to move any cars thereon.

20. Said agreements of January 4, 1909 and

## Exhibit "A"—(Continued)

February 27, 1909 are hereby terminated as of the date hereof.

21. Notwithstanding the foregoing, that certain supplemental agreement between the parties hereto dated August 14, 1940 shall continue in full force and effect during the life of this agreement in the same manner and to the same extent as if this agreement were specifically referred to in Section 7 thereof.

---

EXHIBIT "B"

To Booth-Kelly Lumber Company, a corporation:

## Notice, Demand and Tender

You are hereby notified that on February 8, 1945, at approximately 1:15 p.m. of said day, Mack D. Powers, an employee of Southern Pacific Company, was engaged in switching cars on the spur track on your premises near Springfield Station, County of Lane, State of Oregon. In the course of his employment, he was on or about a railroad car moving along said spur track and was injured by coming into contact with a wood cart which had been left standing near said spur track by you. Southern Pacific Company operated on said spur track, in performance of its duties as a common carrier by railroad for hire.

Heretofore, and on October 2, 1945, said Mack D. Powers, as plaintiff, commenced an action in the Superior Court of the State of California in

and for the City and County of San Francisco against Southern Pacific Company as defendant which said action is entitled and numbered as follows: "Mack D. Powers, plaintiff, vs. Southern Pacific Company, a corporation, defendant," Number 344915. Enlargement of the time for defendant to appear to December 15, 1945 has been obtained. In said action he makes claim against Southern Pacific Company for damages on account of his said injuries, and alleges in substance and effect, that said injuries were proximately caused by the presence of a loaded wood cart so close to the said spur track as to allow insufficient clearance for his body between the wood cart and the caboose. For further particulars of said claim, reference is made to the complaint to the action.

On June 30, 1941, you entered into a contract in writing with the Southern Pacific Company, a corporation. Said contract has been in full force and effect ever since.

It is the position of Southern Pacific Company that the claim of said Mack D. Powers is not chargeable in whole or in part against it; that Southern Pacific Company is not chargeable in whole or in part for liability involved in such claim; and that the injuries and damages of said George S. Price were due to the acts and/or omissions of Booth-Kelly Lumber Company, its officers, agents, servants and employees, and were due to breach of said contract of June 30, 1941 by Booth-Kelly Lumber Company, in leaving said wood cart

in such close proximity to the said spur track as not to allow sufficient clearance, in permitting said wood cart to remain in such position, and in failing to notify Southern Pacific Company and its officers, agents, servants and employees, including said Mack D. Powers, of the presence of said wood cart, as hereinabove described, all without the consent of Southern Pacific Company, and that negligence on the part of Booth-Kelley Lumber Company was active, and any negligence on the part of Southern Pacific Company, if any, was remote and passive only.

It is further the position of Southern Pacific Company that the injuries and damages of said Mack D. Powers were due to the violation and breach by you of the terms, covenants and conditions of said contract of June 30, 1941.

You are required to and demand is hereby made upon you, to indemnify and save harmless Southern Pacific Company and its successors and assigns from and against any and all claims, liability, judgment or judgments, costs, attorneys' fees and expenses of whatever nature, resulting from or by reason of the injuries to said Mack D. Powers and the matters hereinabove referred to. To this end you are hereby notified and required to appear in said action and make defense thereto on account and for Southern Pacific Company, and the defense of said action on behalf of Southern Pacific Company is hereby tendered to you.

In the event you decline said demand and decline



such tender, Southern Pacific Company, not waiving its rights and claims aforesaid, makes further demand upon you that you appear in said action and make defense with Southern Pacific Company jointly, and bear equally with Southern Pacific Company any and all claims, liability, judgment or judgments, costs, attorneys' fees and expenses of whatever nature resulting from or by reason of injuries to said Mack D. Powers and the matters hereinabove referred to.

In any event, demand is hereby made upon you to perform the terms, covenants and conditions of said agreement of June 30, 1941 on your part to be performed.

Will you be kind enough to notify us what action you propose to take. You may notify us by advising our attorney in said action, Arthur B. Dunne, Esq., Room 611, 333 Montgomery Street, San Francisco, California, Telephone Yukon 1977. In the event you undertake the defense of said action on behalf of Southern Pacific Company and agree to indemnify Southern Pacific Company as specified above and so advise Mr. Dunne, such attorneys as you may select will be given appropriate substitutions and the undersigned and its attorneys will cooperate with you and your attorneys in the preparation of said case for trial, and furnish such information as the undersigned has.

Without restricting any of the foregoing and for the purpose of advice to you in the premises, we hereby advise you that one of the positions of

the undersigned is that the wood cart hereinabove referred to, and the cart referred to in the complaint in said action Number 344915 was placed and left by you in the position in which it was at the time of the above referred to accident, in violation of the said agreement of June 30, 1941 and that Southern Pacific Company asserts and will assert all such rights as it has under said agreement and all such rights as it may have irrespective of said agreement.

SOUTHERN PACIFIC  
COMPANY

By D. J. RUSSELL  
Vice President

[Endorsed]: Filed Dec. 19, 1947.

---

[Title of District Court and Cause.]

ANSWER

Comes now defendant and for its Answer to plaintiff's Complaint, admits, denies and alleges:

I.

Admits the allegations contained in Paragraphs I and II of plaintiff's Complaint.

II.

Answering Paragraph V of plaintiff's Complaint, defendant admits that on February 8, 1945, Mack D. Powers was injured while acting in the employ

of plaintiff and riding on a caboose being operated by plaintiff on the spur track referred to in the agreement alleged in Paragraph II of plaintiff's Complaint.

### III.

Answering Paragraphs VI and VII of plaintiff's Complaint, defendant admits that Mack D. Powers brought an action against plaintiff for damages which he received as a result of the negligence of plaintiff and that he recovered judgment against the plaintiff in said action.

### IV.

Answering Paragraph VIII of plaintiff's Complaint, defendant denies that plaintiff has paid any of the sums herein and demands proof thereof.

### V.

Denies each and every allegation as set forth in plaintiff's Complaint excepting such allegations as hereinbefore admitted and excepting such allegations as may be specifically admitted, stated, or qualified in defendant's further and separate and Affirmative Answers and Defenses, which said Affirmative Answers are made a part hereof for the purpose of this denial the same as fully set forth.

### First Affirmative Answer and Defense

Comes now the defendant and for its first separate and affirmative answer and defense, alleges:

## I.

That on or about June 30, 1941 plaintiff and defendant entered into and executed an industrial track agreement prepared by plaintiff covering the maintenance and operation of industrial track facilities serving defendant's Springfield mill, a copy of which agreement is attached to plaintiff's Complaint, marked Exhibit "A" and by this reference is made a part hereof for the purpose of this defense the same as though fully set forth.

## II.

That plaintiff had knowledge of the presence of the wood cart referred to in Paragraph V of plaintiff's Complaint for a period of at least four (4) days prior to February 8, 1945, when Mack D. Powers backed out of the caboose of plaintiff and was carried on said caboose against said wood cart and received certain injuries.

## III.

That plaintiff failed to notify defendant, its employees or agents to move said wood cart and failed to inform defendant of the presence of said wood cart at the place where the above accident occurred.

## IV.

That plaintiff waived any violation of said industrial track agreement with respect to the position of the wood cart.



## Second Affirmative Answer and Defense

Comes now the defendant and for its second separate and affirmative answer and defense, alleges:

## I.

Realleges the allegations contained in Paragraphs I, II and III of its first affirmative answer and defense and by reference incorporates the same herein the same as though fully set forth.

## II.

That plaintiff continued to operate its trains over said spur track after receiving notice of the presence of said wood cart at the place where this accident occurred and assumed the risk of any injury which resulted from the presence of the wood cart near said spur track.

## Third Affirmative Answer and Defense

Comes now the defendant and for its third separate and affirmative answer and defense, alleges:

## I.

Realleges the allegations contained in Paragraph I of its first affirmative answer and defense and by reference incorporates the same herein the same as though fully set forth.

## II.

That on February 8, 1945 Mack D. Powers, while acting in the course of his employment as a brakeman for plaintiff, detrained from a caboose being

operated by plaintiff and was carried by plaintiff into and against a wood cart adjacent to said spur track and receive certain personal injuries.

### III.

That thereafter the said Mack D. Powers brought an action against plaintiff in the Superior Court of the State of California, In and For the City and County of San Francisco, entitled, "Mack D. Powers, plaintiff vs. Southern Pacific Company, a corporation, defendant, #344-915" to recover for said injuries based upon allegations that negligence of plaintiff was the proximate cause of said injuries.

### IV.

That said action came on for trial and resulted in a verdict in favor of said Mack D. Powers and judgment was duly entered in favor of said Mack D. Powers and against Southern Pacific Company.

### V.

That defendant is a corporation organized under the laws of the State of Oregon and is duly authorized to engage in the lumber business.

### VI.

That said agreement, insofar as it purports to bind and make defendant liable as an indemnitor for the negligence of plaintiff as the indemnitee, is illegal and void and contrary to public policy.

#### Fourth Affirmative Answer and Defense

Comes now the defendant and for its fourth separate and affirmative answer and defense, alleges:

##### I.

Realleges the allegations contained in Paragraphs I, II, III, IV and V of its third affirmative answer and defense and by reference incorporates the same herein the same as though fully set forth.

##### II.

That the liability of plaintiff to the said Mack D. Powers was based solely upon the master-servant relation existing between those parties and the duty of plaintiff to exercise due care with respect to said Mack D. Powers, and the liability was not related to and did not arise out of any contractual relation between plaintiff and defendant under said industrial track agreement.

##### III.

That there was no consideration for any promise by defendant to indemnify plaintiff for liability or damage not related to or arising out of or dependent upon the contractual relation between plaintiff and defendant under said industrial track agreement.

#### Fifth Affirmative Answer and Defense

Comes now the defendant and for its fifth separate and affirmative answer and defense, alleges:

## I.

Realleges the allegations contained in Paragraph I of its first affirmative answer and defense and by reference incorporates the same herein the same as though fully set forth.

## II.

That at all times hereinafter mentioned plaintiff was a corporation organized under the laws of the State of Kentucky and doing business in the State of Oregon and other states and was engaged in the business of common carrier by railroad in interstate commerce.

## III.

That on the 8th day of February, 1945 at about the hour of 1:15 o'clock p.m., Mack D. Powers was engaged in the employ of plaintiff as a brakeman and was acting in the course of said employment on a train being operated by plaintiff on said spur track.

## IV.

That at said time and place, Mack D. Powers in detraining from a caboose being operated on said spur track by plaintiff, was carried into and against a wood cart located adjacent to the track, as the result of which accident said Mack D. Powers received certain injuries.

## V.

That at said time and place plaintiff was negligent in that:



(a) It failed to warn Mack D. Powers of the presence of said wood cart.

(b) It failed to furnish Mack D. Powers with a safe place in which to work in that he was required to demount from a side door caboose rather than a rear door caboose.

(c) It failed to properly indoctrinate Mack D. Powers in the proper manner of detraining from a side door caboose.

(d) It failed to remove said wood cart or cause other persons to remove same.

## VI.

That the aforesaid negligence of plaintiff was the sole proximate cause of and contributed to the proximate cause of the injuries to Mack D. Powers.

## VII.

Realleges the allegations contained in Paragraphs III and IV of its third affirmative answer and defense and by reference incorporates the same herein the same as though fully set forth.

### Sixth Affirmative Answer and Defense

Comes now the defendant and for its sixth separate and affirmative answer and defense, alleges:

#### I.

Realleges the allegations contained in Paragraphs I, II, III and IV of its fifth affirmative answer and defense and by reference incorporates the same herein the same as though fully set forth.

## II.

That at said time and place, Mack D. Powers was negligent in that:

(a) He failed to keep a proper lookout.

(b) He backed out of caboose without ascertaining that such move could be made safely.

(c) He attempted to detrain in the proximity of said wood cart.

(d) He backed out of caboose while the train was moving and before it had safely passed said wood cart.

(e) He failed to report the presence of said wood cart adjacent to the track to plaintiff or defendant.

## III.

That said negligence contributed to and was a proximate cause of the injuries received by Mack D. Powers.

Wherefore, defendant prays that plaintiff take nothing by its Complaint and that the defendant have judgment against plaintiff for its costs and disbursements herein.

GRIFFITH, PECK,  
PHILLIPS & NELSON,

By /s/ JAMES K. BUELL,  
Attorneys for Defendant.

Service of copy acknowledged.

[Endorsed]: Filed Jan. 31, 1948.

[Title of District Court and Cause.]

Civil No. 3989

### PRE-TRIAL ORDER

The above entitled action came on regularly for pre-trial conference before the undersigned judge of the above entitled Court on Tuesday, November 9, 1948. The plaintiff appeared by and through Alfred H. Corbett, one of its attorneys. The defendant appeared by and through James A. Powers and James K. Buell, its attorneys. Counsel, with the approval of the Court agreed to the following:

#### Admitted Facts

##### I.

At all times mentioned herein, plaintiff was a corporation domiciled in and organized under laws of the State of Kentucky. On or about September 1, 1947, plaintiff was re-organized as a Delaware Corporation, and removed its domicile to said last named state, and ever since said date has been, and is now a corporation organized under the laws of Delaware. At all times herein mentioned, the plaintiff was, and is engaged as a common carrier by railroad in interstate and intrastate commerce in Oregon. The defendant is an Oregon corporation. The amount in controversy exclusive of interest and costs, exceeds the sum of Three Thousand Dollars (\$3,000).

## II.

On or about June 30, 1941, the plaintiff entered into an Industrial Track Agreement with defendant, covering the maintenance and operation of industrial track facilities serving defendant's Springfield Mill on premises used or owned by defendant, which agreement is marked pre-trial Exhibit 1.

## III.

On February 8, 1945, when said agreement was still in effect, Mack D. Powers was engaged as brakeman for plaintiff as part of the crew of one of plaintiff's trains which was switching over the industrial track covered by said agreement, delivering cars. The train was under the general direction of a conductor. While so engaged, and while detraining from the caboose, Mack D. Powers was injured by being caught between the side of the caboose and a wood cart which was the property of defendant and had been placed and left by the defendant, its employees or agents alongside said track in such a position that one corner of the cart was 42" from the outside edge of the outside rail of said track.

## IV.

Said employee brought action against Southern Pacific Company for damages for his injuries under the provisions of the Federal Employer's Liability Act. The complaint alleged breach of Southern Pacific Company's statutory duty of using ordinary care to provide said Mack D. Powers with a reason-



ably safe place in which to work in that, first, it caused and permitted the wood cart to remain on the track, and second, it failed to warn him of the presence of the wood cart and the resultant insufficient clearance.

At trial the allegation that Southern Pacific Company placed the wood cart on the track was removed from the jury's consideration because of lack of evidence. A verdict was returned for said Mack D. Powers.

The records of said proceeding, consisting of pleadings, transcript of proceedings at trial, verdict and judgment are marked pre-trial Exhibits 2a to 2g, both inclusive.

## V.

Shortly after the filing of said action against it by Mack D. Powers, and before time for answer, plaintiff gave notice and made demand and tender of defense upon defendant, which Notice, Demand and Tender is marked pre-trial Exhibit 3. Defendant denied any liability arising out of said accident and refused to assume the defense to said action.

## VI.

Subsequent to the rendering of the judgment against it, after agreement with defendant that such settlement should be without prejudice to its contention that defendant was obligated to pay the amount of said judgment, and plaintiff's costs and similarly without prejudice to any contentions on the part of defendant that it was not obligated to

pay anything by reason of said accident or judgment, plaintiff compromised said judgment by the payment to Mack D. Powers of the sum of \$44,699.46. Satisfaction of judgment showing payment of said sum is marked pre-trial Exhibit 4.

## VII.

In addition to said sum, which plaintiff paid Mack D. Powers, plaintiff was obligated to pay, and has paid One Thousand Eight Hundred Sixty-nine Dollars and Fifty-three Cents (\$1,869.53) for costs and attorneys' fees in defending said action of Mack D. Powers.

## VIII.

Subsequent to the payment of said sums, plaintiff made demand upon defendant for the payment thereof, which sums defendant failed and refused, and still refuses to pay.

## IX.

It is agreed that both parties to this action are bound by the proceedings and judgment in the action, Mack D. Powers v. Southern Pacific Company as to all matters there determined.

## Contentions of the Parties

### A.

Plaintiff contends defendant breached said Industrial Track Agreement by placing and leaving its wood cart within 42" from the track; that as the natural or necessary result of defendant's said

breach of contract plaintiff was damaged in the sum of \$46,568.99; and that plaintiff is entitled to receive said sum from defendant as damages for breach of contract.

With respect to plaintiff's A,

Defendant admits that one of its wood carts was left within a distance of 42 inches from the nearest rail of the said track, but denies that this constitutes a breach of said agreement which would impose liability on this defendant for the loss plaintiff sustained for the reasons:

(1) That under said agreement plaintiff railroad was given full control over the said track and said plaintiff railroad had the right to regulate all trains and the right to have any obstructions removed which interfered with the railroad's operations and which in the railroad's judgment were deemed hazardous or dangerous.

(2) That the wood cart was in the same place it was in when the accident occurred approximately from January 30 to and including February 8, the date of the accident, and this with the full knowledge, consent and approval of the plaintiff railroad company who, acting through its agents and employees and men operating its trains, was fully aware of the condition as it existed, and plaintiff was in the best position to know of any hazard or danger created by the cart, but nevertheless continued to operate and run its trains with full knowl-

edge that said wood cart was standing at said distance from the track.

(3) Defendant denies that there was any breach of said track agreement, but if there was a breach there was a waiver thereof by the plaintiff railroad company through its continued operation of its trains with full knowledge of existing conditions, and moreover such breach, if any, was not the cause of plaintiff's loss and the agreement does not cover and was not intended to cover a loss resulting through plaintiff's own negligence nor to allow plaintiff railroad company to recover for a loss which it sustained through its own negligence.

(4) The agreement referred to is one of several entered into by the parties covering the same track, and it should be considered together with the earlier agreements in order to show the entire transaction; that there is no consideration for the additional obligations contained in the agreement of June 30, 1941, under which plaintiff seeks to recover herein.

(5) A custom was developed by the parties under the track agreement to the effect that the railroad would notify the defendant whenever there was any obstruction of the track clearance and defendant would remove same, and the railroad having failed to follow the customary practice is estopped by its conduct from asserting that the alleged breach caused the loss.

(6) A breach, if any, as to clearances under the track agreement would not in any event give rise



to a cause of action for any damages resulting therefrom, since paragraph (9) of the agreement expressly provides that railroad shall have a right to discontinue service in that event.

(7) Defendant contends that even if there has been a breach of clearances under the contract, and even if plaintiff would ordinarily be entitled to damages resulting from such a breach, it is not in this case for the reason that the breach was discovered by plaintiff prior to damage and therefore such damage was not caused by the claimed breach.

(8) That plaintiff would not be entitled to recover costs and attorneys fees incurred in California action under a breach of the contract theory.

(9) That the railroad company failed to put a sign in the converted caboose warning trainmen of the danger descending therefrom in a backward manner without first looking to see that the way was clear.

Plaintiff denies the foregoing.

### B.

As an alternative to A, plaintiff contends that it has been obligated to pay \$46,568.99 by reason of injury to one of its employees occasioned by an act or omission of defendant while the employee was on or about the industrial track, and that under the Industrial Track Agreement defendant is obligated to indemnify and hold harmless the plaintiff in that amount.

With respect to plaintiff's contention B, defendant contends:

(1) That the payment made by the plaintiff railroad company did not result from an act or omission of the defendant but was the result of plaintiff's own act or omission as established and adjudicated in the California action in which it was held that an act or omission of plaintiff's caused the injuries to its employee or that the combined act or omission of the plaintiff and its employee Mack D. Powers caused his injuries with the resultant loss to plaintiff railroad. The plaintiff is not entitled to recover from the defendant under said industrial track agreement for a loss sustained through its own act or omission, or through its act or omission combined with that of another.

(2) No consideration for the agreement to indemnify and hold harmless; that the same was obtained after the spur track and agreement was in operation and without any consideration therefor moving to defendant.

(3) To uphold plaintiff's contention would permit plaintiff as a common carrier to enforce indirectly a contract, which under the circumstances here is void as against public policy.

(4) Defendant contends that plaintiff's liability to Powers did not arise out of the track agreement but rather out of the master-servant relationship between itself and Powers and under the Federal-

Employers Liability Act and that therefore the indemnity provision of the track agreement would not cover this liability.

(5) Defendant contends that extension of the indemnity agreement to cover subject case would be contrary to public policy and void in that plaintiff would be thereby enabled to escape liability for a breach of its non-delegable duty under the Federal Employers Liability Act.

(6) Defendant contends that plaintiff had an affirmative duty under the track agreement to exercise due care in the operation of its trains over subject track and that its breach of said duty is a breach of a condition of the agreement which forfeits right of plaintiff to require performance of the indemnity provision of the agreement by defendant.

(7) Defendant also reasserts its contentions hereunder that were made under plaintiff's contention "A".

Plaintiff denies the foregoing.

### C.

As an alternative to A and B, plaintiff contends that defendant is obligated to pay plaintiff \$46,568.99 since defendant's negligence was the active or primary cause of the injury to plaintiff's employee, Mack D. Powers.

With respect to plaintiff's contention C, defendant contends:

(1) Defendant denies that it is in any way obligated to pay plaintiff railroad company the sum claimed, and defendant contends that plaintiff is estopped by the judgment in the California action from asserting that the loss that plaintiff sustained resulted from anything other than its own negligence which proximately caused the accident and injuries. It was established in that action that it was plaintiff's own negligence in operating its train under conditions fully known to it which was the immediate proximate cause of the accident and injuries.

(2) Defendant contends that plaintiff is not entitled to enforce contribution from an alleged joint tortfeasor.

(3) That if it should become an issue under any of plaintiff's contentions as to whether plaintiff's negligence caused the loss and injury to Mack D. Powers or whether plaintiff's negligence was a contributing cause of said injuries and loss, defendant then contends that the railroad was negligent in the following particulars:

(a) In operating its train knowing of the impaired clearance and particularly with knowledge that it was using a converted box car for a caboose which was so constructed it required a person descending from the caboose or box car to the ground to do so in a backward movement.

(b) In using a converted box car for a caboose which was so constructed as to require a person



descending from the caboose to do so in a backward manner and in such manner that a person descending could not see where he was going or what his body might strike.

(c) In failing to observe the rules and regulations with respect to operating trains and particularly with respect to causing any obstructions which impaired clearances to be removed.

(d) In operating its train with full knowledge that there was an impaired clearance which created a hazard or danger for the trainment.

(e) In failing to furnish its employees a safe place to work.

(f) In failing to notify defendant to remove the obstruction.

(g) In operating its train knowing of the hazardous condition and in failing to warn employees thereof, and particularly Mack D. Powers.

(h) That the railroad was aware of the dangerous and hazardous condition which being known to it, the railroad had a last clear chance of avoiding the accident and it was negligent in failing to stop the train which it had an opportunity to do before an accident occurred to require said obstruction to be removed.

(i) That the agent and employee of the defendant, Mack D. Powers was then and there negligent in failing to look before he attempted to descend

from the train and in riding on the train in the switching operations, in failing to see the alleged obstruction, in failing to comply with the rules and regulations of the railroad company, and in placing himself in a dangerous position when a safe position was open to him.

(4) Defendant further contends that plaintiff's negligence was established in the California trial between Mack D. Powers and the plaintiff and that the proximate cause of the accident and injuries was established in said action as being the negligence of the Southern Pacific Company and not the negligence of this defendant, and this defendant's negligence, if any, was a remote cause and not an immediate proximate cause; that the matter is now *res adjudicata*.

Plaintiff denies the foregoing, and further contends that if it is determined that plaintiff was guilty of negligence which proximately caused the injury to Mack D. Powers, and if it is determined that plaintiff is not otherwise entitled to recover the full amount of \$46,568.99, defendant was likewise guilty of negligence which was a joint or concurring cause of the damage to Powers and resulting liability of plaintiff, and under the agreement defendant must, in any event, assume one-half the cost and must pay plaintiff \$23,284.49.

### Issues of Fact

1. Was the damage to Powers and liability of plaintiff the natural or necessary result of defend-

ant's breach of contract? If so, in what amount?

2. Was plaintiff damaged by reason of an act or omission of defendant, its agents or employees to an employee of plaintiff while on or about the industrial track? If so, in what amount?

3. Was defendant negligent in placing and leaving the wood cart within 42" from the track? If so, was defendant's negligence in this regard the active or primary cause of the injury to plaintiff's employee, Powers?

4. Did the damage to plaintiff's employee arise from the joint or concurring negligence of plaintiff and defendant?

5. Was it established in the California trial and proceedings that the plaintiff through violation of the Federal Employers Liability Act was negligent and that its negligence proximately caused the injuries to Powers and the resulting loss?

6. Is the matter of the railroad company's negligence as determined in the California proceedings and trial res adjudicata? If not, was the railroad company negligent in any of the particulars specified in defendant's contentions?

7. Was the negligence of Booth-Kelly, if any, remote?

8. Was there any consideration for the indemnity provision contained in the track agreement?

9. Is plaintiff barred from recovering under the track agreement by reason of its own acts and conduct?

10. Was there a custom and practice between the parties under which plaintiff would give notice to defendant of any objectionable obstruction to track clearance, and a further custom of defendant's removing same at the request of railroad?

11. Did plaintiff discover the alleged breach prior to the accident and if so was the loss and damage caused by plaintiff's conduct in continuing operations without taking steps to have the cart removed or to warn its employees thereof?

### Issues of Law

A. Was the placing and leaving of the wood cart within 42" from the track a breach of contract by defendant?

B. Is plaintiff entitled to be indemnified by defendant under the industrial track agreement in the sum of \$46,568.99 or any part thereof?

C. Is defendant obligated plaintiff \$46,568.99 or any part thereof independent of the agreement?

D. Can an employer under the Federal Employers Liability Act delegate the duties imposed upon him by said Act?

E. Is the negligence imposed upon an employer for violation of the Federal Employers Lia-



bility Act resulting in injuries to an employee considered to be primary negligence?

F. Can a railroad operating as a common carrier contract to be held harmless against its own negligence or is such contract void as against public policy.

G. Whose control was the track under and did the track area include the point and place where the cart was located?

H. Did the railroad have the right to have any obstructions removed which railroad deemed hazardous?

I. Was there a waiver of any breach if one existed?

### Exhibits

The following exhibits were received and marked as pre-trial exhibits, the parties agreeing that no further identification or authentication is necessary. All objections are waived as to Pre-trial Exhibits, 1, 2a to 2g, both inclusive, 3, 4, 5, 6 and 7. In the event any or all the other exhibits are offered in evidence at the time of trial, said exhibits are to be subject to objection only upon the grounds of materiality, competency or relevancy:

Plaintiff's Exhibit 1.—Industrial track agreement dated June 30, 1941.

Plaintiff's Exhibit 2a.—Copy or complaint, Mack D. Powers against Southern Pacific Company.

Plaintiff's Exhibit 2b.—Copy of answer, Powers v. Southern Pacific Company.

Plaintiff's Exhibit 2c.—Transcript, Powers v. Southern Pacific Company, January 28, 1947.

Plaintiff's Exhibit 2d.—Transcript, Powers v. Southern Pacific Company, January 29 and 30, 1947.

Plaintiff's Exhibit 2e. — Transcript, Powers v. Southern Pacific Company, January 31, 1947.

Plaintiff's Exhibit 2f.—Copy of verdict, Powers v. Southern Pacific Company.

Plaintiff's Exhibit 2g.—Copy of judgment on verdict, Powers v. Southern Pacific Company.

Plaintiff's Exhibit 3.—Notice, Demand and Tender.

Plaintiff's Exhibit 4.—Satisfaction of judgment, Powers v. Southern Pacific Company.

Plaintiff's Exhibit 5.—Picture of cart taken shortly after accident, looking west.

Plaintiff's Exhibit 6.—Picture of cart taken shortly after accident, looking east.

Plaintiff's Exhibit 7.—Picture of caboose taken shortly after accident.

Defendant's Exhibit 8.—Spur track agreement dated 1902.

Defendant's Exhibit 9.—Spur track agreement dated 1-4-1909.

Defendant's Exhibit 10.—Spur track agreement dated 2-27-1909.

Defendant's Exhibit 11.—Spur track agreement dated 8-14-1940.

Defendant's Exhibit 12.—Spur track agreement dated 8-15-1940.

Defendant's Exhibit 14.—Copy General Safety Rules of Southern Pacific Company.

Defendant's Exhibit 15.—Copy Rules & Regulations for the maintenance of Way & Structures of Southern Pacific Company #4621.

Defendant's Exhibit 16.—Letter from plaintiff to defendant, June 6, 1940.

Defendant's Exhibit 17.—Letter from plaintiff to defendant, February 5, 1940.

Defendant's Exhibit 18.—Picture of side door caboose taken February 12, 1945.

The foregoing is a Pre-trial Order agreed upon at a conference between counsel and the Court. It shall not be amended at the trial except by consent or to prevent manifest injustice. It is ordered that this Pre-trial Order supersedes the pleadings which now pass out of the picture.

No demand for jury trial was made by either party.

The foregoing Pre-trial Order is hereby approved and entered this 11th day of November, 1948.

/s/ JAMES ALGER FEE,  
Judge.

Order Approved:

/s/ ALFRED H. CORBETT,  
Of Attorneys for Plaintiff,  
/s/ JAMES ARTHUR POWERS,  
Of Attorneys for Defendant.

[Endorsed]: Filed Nov. 11, 1948.

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In the United States District Court  
for the District of Oregon

Civil No. 3989

SOUTHERN PACIFIC COMPANY,  
a Corporation,

Plaintiff,

vs.

BOOTH-KELLEY LUMBER COMPANY,  
a Corporation,

Defendant.

FINDINGS OF FACT AND CONCLUSIONS  
OF LAW

The above entitled action came on regularly for trial in the above entitled court on November 11, 1948, plaintiff appearing by Alfred H. Corbett, one



of its attorneys, and defendant appearing by James Arthur Powers, one of its attorneys, and witnesses having been sworn and evidence submitted, and the court having considered the various issues of law and of fact now makes the following:

### Findings of Fact

1. Plaintiff is a Delaware corporation. Previous to September 1, 1947, when plaintiff was reorganized, plaintiff was a corporation domiciled in and organized under the laws of the State of Kentucky, and at all times pertinent to this case, was engaged as a common carrier by railroad in interstate and intrastate commerce in Oregon. Defendant is an Oregon corporation. The amount in controversy exclusive of interest and costs, exceeds the sum of \$3,000.00.

2. On or about June 30, 1941, plaintiff entered into an industrial track agreement with defendant, covering the maintenance and operation of industrial track facilities serving defendant's Springfield mill on premises used or owned by defendant.

3. On February 8, 1945, when agreement was still in effect, Mack D. Powers was engaged as brakeman for plaintiff as part of the crew of one of plaintiff's trains which was switching over the industrial track covered by said agreement, delivering cars. The train was under the general direction of a conductor. While so engaged, and while detraining from the caboose, Mack D. Powers was injured by being caught between the side of the

caboose and a wood cart which was the property of defendant and had been placed and left by the defendant, its employees or agents alongside said track in such a position that one corner of the cart was 42 inches from the outside edge of the outside rail of said track.

4. Said employee brought action against Southern Pacific Company for damages for his injuries under the provision of the Federal Employers Liability Act. The complaint alleged breach of Southern Pacific Company's statutory duty of using ordinary care to provide said Mack D. Powers with a reasonably safe place in which to work in that, first, it caused and permitted the wood cart to remain on the track, and second, it failed to warn him of the presence of the wood cart and the resultant insufficient clearance.

At trial the allegation that Southern Pacific Company placed the wood cart on the track was removed from the jury's consideration because of lack of evidence. A verdict was returned for Mack D. Powers.

5. Shortly after the filing of said action against it by Mack D. Powers, and before time for answer, plaintiff gave notice and made timely demand and tender of defense upon defendant. Defendant denied any liability arising out of said accident and refused to assume the defense to said action.

6. Subsequent to the rendering of the judgment against it, after agreeing with defendant that such

settlement should be without prejudice to its contention that defendant was obligated to pay the amount of said judgment, and plaintiff's costs and similarly without prejudice to any contentions on the part of defendant that it was not obligated to pay anything by reason of said accident or judgment, plaintiff compromised said judgment by the payment to Mack D. Powers the sum of \$44,699.46.

7. In addition to said sum plaintiff was obligated to pay and has paid \$1,869.53 for costs and attorneys' fees in defending said action of Mack D. Powers.

8. Subsequent to the payment of said sums, plaintiff made demand upon defendant for the payment thereof which sums defendant refused to pay.

9. Defendant was negligent in placing and leaving the wood cart within 42 inches from the spur track.

10. Defendant's negligence in this regard was the active, direct, proximate and primary cause of the injury to plaintiff's employee Powers.

11. Powers suffered injuries in the amount of \$44,000.00.

12. Plaintiff suffered loss in the amount of \$44,699.46 judgment costs and of \$1,869.53 court costs and attorneys' fees, by reason of an act or omission of defendant, its agents or employees to an employee of plaintiff while on the industrial track.

13. The damage to Powers and the liability of

plaintiff was the natural or necessary result of defendant's breach of contract.

14. Some elements of negligence on the part of plaintiff concurred to cause the accident.

15. Plaintiff was not negligent in the form of the specifications of negligence made by defendant in the pre-trial order.

16. There was consideration for the indemnity provisions of the spur track agreement.

17. Employees of plaintiff observed the position of the cart and operations continued thereafter prior to the accident.

18. The loss and damage to Powers were not proximately caused by the conditions mentioned in the previous findings.

19. There was no custom or practice between the parties under which plaintiff would give notice to defendant of any objectionable obstruction to track clearance or of defendant moving the same at the request of the plaintiff.

20. This case involves different parties and different issues than were presented in the action of Mack D. Powers against plaintiff.

21. The placing and leaving of the wood cart within 42 inches from the track was a breach of the provisions of said agreement relating to impaired clearances.

Based on the foregoing finds of fact the court hereby makes and enters the following:



Conclusions of Law

1. The industrial spur track agreement is a valid contract.

2. The determinations in the Mack D. Powers' action against plaintiff are not res adjudicata in this proceeding.

3. Plaintiff did not waive defendant's breach of contract.

4. The matter of control over the spur track has no material bearing upon the determination of this case.

5. Defendant is not obligated to pay plaintiff \$44,568.99, or any part thereof, independent of the industrial spur track agreement.

6. Plaintiff had the right under the industrial track agreement to have any obstructions removed which it deemed hazardous.

7. Plaintiff is entitled to recover judgment against defendant for the sum of \$22,000.00 on the contract, together with its costs and disbursements incurred herein.

Dated this 22nd day of June, 1949, at Portland, Oregon.

/s/ JAMES ALGER FEE,  
Judge.

Service of copy acknowledged.

[Endorsed]: Filed June 22, 1949.

In the United States District Court  
for the District of Oregon

Civil No. 3989

SOUTHERN PACIFIC COMPANY,  
a Corporation,

Plaintiff,

vs.

BOOTH-KELLEY LUMBER COMPANY,  
a Corporation,

Defendant.

### JUDGMENT ORDER

The above entitled action having come on for trial on the Pre-trial Order and proofs of the respective parties, and having been argued by counsel for the parties, and the court after deliberation having heretofore signed and entered findings of fact and conclusions of law, it is now

Ordered and Adjudged that plaintiff have and recover judgment against defendant in the sum of \$22,000.00 and for its costs and disbursements herein incurred taxed at \$27.64, and that execution issue therefor.

Dated at Portland this 22nd day of June, 1949.

/s/ JAMES ALGER FEE,  
District Judge.

Service of copy acknowledged.

[Endorsed]: Filed June 22, 1949.

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice Is Hereby Given that the Booth-Kelley Lumber Company, a corporation, the above-named defendant, hereby appeals to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment and the whole thereof, entered in this action on the 22nd day of June, 1949, and which judgment is now final.

By /s/ JAMES ARTHUR POWERS, of  
VEAZIE, POWERS & VEAZIE,  
Attorneys for Appellant.

Service of copy acknowledged.

[Endorsed]: Filed July 22, 1949.

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[Title of District Court and Cause.]

NOTICE OF CROSS-APPEAL

Notice is hereby given that Southern Pacific Company, plaintiff above named, cross-appeals to the Court of Appeals for the Ninth Circuit from so much of the judgment entered in this action on June 22, 1949, as disallows \$24,568.99 of plaintiff's claim.

KOERNER, YOUNG, SWETT &  
McCOLLOCH,  
JAMES C. DEZENDORF,  
ALFRED H. CORBETT,  
Attorneys for Cross-Appellant.

Service of copy acknowledged.

[Endorsed]: Filed July 22, 1949.

United States District Court  
District of Oregon

Civil No. 3989

SOUTHERN PACIFIC COMPANY,  
a Corporation,

Plaintiff,

vs.

BOOTH-KELLY LUMBER COMPANY,  
a Corporation,

Defendant.

Before: Honorable James Alger Fee,  
Judge.

Appearances:

ALFRED H. CORBETT,  
KOERNER, YOUNG, SWETT &  
McCOLLOCH,  
of Attorneys for Plaintiff.

JAMES ARTHUR POWERS,  
VEAZIE, POWERS & VEAZIE,  
of Attorneys for Defendant.

### TRANSCRIPT OF PROCEEDINGS

Mr. Corbett: We are agreed upon a pre-trial order, your Honor. There is just one matter. We have crossed out several words by way of changes that were made. Defendant's Exhibit No. 13 was



reserved for a map. Could that be entirely eliminated, if there is no Exhibit No. 13, or does that show the exhibit number?

The Court: No, just strike it out.

Mr. Corbett: Strike it out entirely?

The Court: Yes.

(Proposed Pre-Trial Order handed to the Court.)

The Court: The pre-trial order is signed and entered.

Mr. Corbett: If the Court please, this case is a case brought by the Southern Pacific Company to recover over against the Booth-Kelly Lumber Company the amount necessary to satisfy a judgment and the amount paid as attorney's fees and costs for a judgment against Southern Pacific Company by Mack D. Powers, one of the Southern Pacific Company's employees.

Mack D. Powers was injured while working on an industrial spur track serving defendant's mill. The track was on premises used or owned by the defendant.

The evidence will show in this case, or will tend to show, that the accident happened February 8, 1945. Mr. Powers was the rear brakeman of a crew on Southern Pacific's work extra 3904. That train was serving the Springfield area. After several switching movements, which are not important

here, the crew undertook to deliver five cars of logs on this industrial spur serving the defendant.

I am informed this morning by opposing counsel that the logs were not delivered to the defendant, Booth-Kelly Lumber [2\*] Company. However, they were delivered over this spur track which is covered by the agreement. The position of the car in question will be shown, if the Court would look at the map which is attached to Pre-Trial Exhibit No. 1, and which I understand may be offered in evidence following this statement, if that is agreeable to Counsel——

Mr. Powers: Yes.

Mr. Corbett: The spur track in question takes off near the station to the west and runs down a distance of approximately 2200 feet.

On the day in question, after the switching operations, the train was pushing five log cars to spot them up in the vicinity of the crane setout spur. The engine was headed east. Ahead of the engine was the caboose and these five cars were ahead of the caboose.

The train pushed the cars down and spotted them in approximately the middle of the spur track. Then the engine and caboose were going to proceed back, and near the west end of the spur,—that is, near its commencement,—they were to cut off the caboose and leave the caboose in position while the engine switched and did some other work.

After spotting the cars the engine and caboose

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\* Page numbering appearing at top of page of original Reporter's Transcript.

proceeded back towards the west end of the track and at a point between 350 and 400 feet from the westerly end of the spur, Mack D. Powers was de-training from the side-door caboose and [3] he was struck by a wood cart, a loaded wood cart, which was the property of the defendant, and which had been placed and left by the defendant for its servants in such position that one corner of the cart was forty-two inches from the outside edge of the outside rail of the track. The caboose overhang was a little over two feet, so there was only approximately fourteen inches, I believe, clearance—about sixteen inches clearance.

Mack D. Powers was seriously injured and subsequently he brought an action against the Southern Pacific Company, alleging that the Southern Pacific Company violated its statutory duty of providing him with a reasonably safe place in which to work. He brought the action in two counts. The first count was that the Southern Pacific Company, or its employees, negligently caused the wood cart to remain on the track; the second count alleged that the Southern Pacific Company or its employees failed to warn him of the presence of the wood cart and resulting insufficient clearance.

I believe the evidence in this case will show, your Honor, that at the trial of Mack D. Powers' case the trial court removed the first count from the consideration of the jury. A verdict was returned for Mack D. Powers, I believe, on the second count; that is, that the Southern Pacific Company failed

to warn Powers of the presence of the wood cart and the insufficient clearance. [4]

After judgment and after a stipulation between the parties that the settlement should be without prejudice to either party, the action was settled for \$44,699.40. The Southern Pacific Company incurred costs and attorney's fees in defending the Powers' action of \$1,869.53, making a total of \$46,568.99.

The Southern Pacific Company has brought this action in three alternative counts, under any one of which we claim the Southern Pacific Company is entitled to receive the full amount, \$46,568.99.

The first count is based upon the industrial track agreement, in that defendant breached the industrial track agreement by placing and leaving its wood cart to within forty-two inches of the track and that, as a necessary or natural result of the breach, the Southern Pacific Company was damaged in that sum. This count concerns Paragraph 5 of the industrial track agreement.

The second count is that the plaintiff has been obligated to pay \$46,568.99 by reason of the injury to one of its employees occasioned by an act or omission of defendant while the employee was on or about the industrial track, and that under the industrial track agreement defendant is obligated to indemnify and hold harmless the plaintiff in that amount, the plaintiff, Southern Pacific Company. That count concerns Paragraph 7 and Paragraph 18. [5]

As the third alternative count, we contend the de-



fendant is obligated to pay the plaintiff \$46,568.99 since defendant's negligence was the active or primary cause of the injury to plaintiff's employee, Mack D. Powers. It is our feeling, your Honor, that upon the industrial track agreement and the proceedings in the Powers case, we are entitled to recover on one of these three theories; that any other evidence is not necessary and we are, as set out in the pre-trial order, bound by whatever is shown in that case.

Our rights are based upon the fact that we have been held liable to an employee at a time when we were operating over that track and we must stand on that liability and on the facts of that case to recover over against the Booth-Kelly Lumber Company.

It has been agreed in the pre-trial order that all objections are waived as to Pre-Trial Exhibits No. 1, No. 2a to No. 2g, both inclusive; No. 3, No. 4, No. 5, No. 6 and No. 7, and at this time I offer in evidence Plaintiff's Exhibit No. 1, the industrial track agreement dated June 30, 1941; Plaintiff's Exhibit No. 2a, copy of the complaint in the case of Mack D. Powers v. Southern Pacific Company; Exhibit No. 2b, copy of answer, Powers v. Southern Pacific Company; Plaintiff's Exhibit No. 2c, transcript, the first volume of the transcript in Powers v. Southern Pacific Company, January 28, 1947; Plaintiff's Exhibit No. 2d, transcript, Powers v. Southern Pacific Company, [6] January 29 and 30, 1947; Exhibit No. 2e, transcript, Powers v. South-

ern Pacific Company, January 31, 1947, which is the Charge of the Court; Exhibit No. 2f, copy of verdict, Powers v. Southern Pacific Company; Exhibit No. 2g, copy of Judgment on Verdict, Powers v. Southern Pacific Company; Plaintiff's Exhibit No. 3, Notice, Demand and Tender; Plaintiff's Exhibit No. 4, Satisfaction of Judgment, Powers v. Southern Pacific Company; Plaintiff's Exhibit No. 5, picture of cart taken shortly after the accident, looking west, towards the commencement of this spur track; Plaintiff's Exhibit No. 6, picture of cart taken shortly after the accident, looking east along the spur track; and Plaintiff's Exhibit No. 7, picture of the side-door caboose which also was taken shortly after the accident.

Mr. Powers: We have no objection to the introduction of any of the exhibits.

The Court: Admitted. They may be marked later.

### Plaintiff's Exhibits

(The following Plaintiff's Pre-Trial Exhibits were thereupon received in evidence and marked as follows:)

Exhibit No. 1—Industrial Track Agreement, dated June 30, 1941.

Exhibit No. 2a—Copy of Complaint, Mack D. Powers v. Southern Pacific Company.

Exhibit No. 2b—Copy of Answer, Powers v. Southern Pacific Company. [7]

Exhibit No. 2c—Transcript, Powers v. Southern Pacific Company, January 28, 1947.

Exhibit No. 2d—Transcript, Powers v. Southern Pacific Company, January 29 and 30, 1947.

Exhibit No. 2e—Transcript, Powers v. Southern Pacific Company, January 31, 1947.

Exhibit No. 2f—Copy of Verdict, Powers v. Southern Pacific Company.

Exhibit No. 2g—Copy of Judgment on Verdict, Powers v. Southern Pacific Company.

Exhibit No. 3—Notice, Demand and Tender.

Exhibit No. 4—Satisfaction of Judgment, Powers v. Southern Pacific Company.

Exhibit No. 5—Picture of cart taken shortly after accident, looking west.

Exhibit No. 6—Picture of cart taken shortly after accident, looking east.

Exhibit No. 7—Picture of caboose taken shortly after accident.

Mr. Corbett: The plaintiff rests, your Honor. [8]

#### Defendant's Motion For Nonsuit

Mr. Powers: The defendant will move for a nonsuit, your Honor, at this time, based upon the proposition that from the exhibits received in evidence, on No. 2c, No. 2d and No. 2e which together make up the transcript of the proceedings in the

trial of the case of Powers against Southern Pacific Company in the California court, and the judgment entered thereon as it appears from the record here, and in so far as that record decided matters present in this action, it appears, your Honor, that the primary negligence was found to be on the Southern Pacific Company; it appears that the case was submitted to the jury and all the testimony there was concerning the negligent acts of the Southern Pacific Company, and it appears from the rules and regulations for maintenance, and the safety rules, and with particular reference to obstructions and impaired track clearance, there is a duty on the part of the railroad; and, further, it appears that the action was brought under the Federal Employers Liability Act and that the jury found, under instructions of the Court, specifically that negligence of the Southern Pacific Company proximately caused the injury complained of; and judgment was entered on the basis that the Southern Pacific's negligence was the proximate cause of the injury, or the Southern Pacific's negligence combined with the negligence of the injured man, proximately caused the accident, and a specific instruction was given to the jury to the effect that the injured man could [9] not recover from the Southern Pacific Company in the event that the jury would find that the negligence of the defendant here, the Booth-Kelly Lumber Company, was the sole proximate cause of the accident or a contributing proximate



cause of the accident, together with that of the injured man himself.

The case was submitted to the jury on two grounds, that the Southern Pacific Company had violated the provisions of the Federal Employers Liability Act, in that they were obligated to furnish employees with a safe place in which to work, and the evidence there showed, and it does show, that the railroad company had knowledge of the cart being in the place that it was in at the time that Powers was struck; it shows that Powers, while attempting to descend from the converted boxcar being used as a caboose, in a backward manner, was required, under the evidence shown, to get out of the boxcar, used as a caboose, in a backward manner and, in doing so, while the train was going at a speed of five miles an hour, this accident occurred.

The evidence shows, too, that this switching operation in which Powers was a brakeman had been going on while the cart was in that same location, for a period of from January 30th until February 8th, when the accident occurred. That was the longest time given by any witness, and the other testimony indicates that one of the men had seen it there for three or four days. The evidence will show from the transcript of testimony that on the day this accident occurred, and before the accident occurred, while this switching operation was in progress [10] that the fireman on this train on the engine, told the engineer about this cart and said, "You can't get by it. You are blocked," and the

engineer, according to the testimony, said, "Well, I got by it before and I know I can clear it."

The evidence further shows in the California case that there were either five or six gondolas or flat-cars loaded with logs. The engine was on one end of the train and the caboose next to the engine and the logs beyond the caboose. As this switching operation started into the premises referred to here, the loads of logs went first. Powers was on the first car of logs. The logs were shunted to a location or spotted near the pond. There was another brakeman standing on top of the caboose as it came along and I think another brakeman on the front of the engine. There was the engineer, of course, operating the train and there was the fireman who called out to the engineer about this obstruction that he could not get by. The conductor testified, now, as I recall it, that the impaired clearance was there.

After the logs had been spotted, five or six cars, they were left there and Powers then got into the caboose which was next to the engine. The engine then was in the process of pulling back to the main line to leave the premises or leave this siding.

With the caboose next to the engine, the engine and caboose were proceeding at the rate of about five miles an hour. [11] Powers then proceeded to get out of the caboose by backing out, and then is when the accident occurred.

The rules of the Southern Pacific were in evidence and they are specific on the point that when there is an impaired clearance the trainmen must

take immediate steps to remove the obstruction; if they cannot handle it locally, they are to notify, by wire if necessary, immediately, the station agent or the railroad master. Actually, at the time this accident occurred, the conductor had left the train, knowing that an impaired clearance was there, and was down at the station. No one gave any notice to the Booth-Kelly Lumber Company to move this cart, and the evidence shows, your Honor, that the cart we are speaking of was a wood cart, mounted, I believe, on iron wheels, and it was used for picking up kindling at the sawmill, short lengths of kindling used to start fires and so forth. There is no evidence that anyone in authority knew the cart was in position, as far as the Booth-Kelly Lumber Company was concerned. It is admitted here it was put or placed there by an employee of the Booth-Kelly Lumber Company, however, so we submit under those facts and under the law and under the agreement we are entitled to a nonsuit now.

I call your Honor's attention to the case of *Layman v. Southern Pacific*, 173 Ore. 275, and also to the case of *Reimers v. Glens Falls*, 176 Ore. 47.

In that latter case I call your Honor's particular attention [12] to the part of the decision which says or stands for the proposition that a violation of the Employers' Liability Act of Oregon constituted the primary negligence in the case. Here, the Southern Pacific Company was held liable by reason of the violation of the Employers' Liability Act

and, under the law, you can't delegate that duty; the employer cannot escape that duty.

Under the Layman case our situation is much more favorable to the defendant, so I believe, than was present in the Layman case, for the reason that the indemnity provision in the Layman case was contained in an agreement in the nature of a license by which the railroad was to get no benefit whatever. They permitted a farmer to cross over their tracks and, in agreeing to let the farmer cross over their tracks, they put in the agreement a provision that the farmer would hold the railroad harmless and indemnify the railroad from loss arising from whatsoever nature, as I recall the language. It was a very broad provision.

That differs from our case here where there was a benefit to the railroad, under this spur track agreement. The railroad, in the first place, was getting the freight, as is shown by the agreement. The railroad, in the second place, reserved and had the right, the contractual right to use this track, this particular spur track, for its own trackage. It could use this track for hauling or delivering logs to others; [13] it could use this track for hauling their freight, freight not belonging to Booth-Kelley Lumber Company; it could use this track for its own purposes, and so on, so that we have a much stronger position here than in that other case.

The Supreme Court in the Layman case did not hold, as I read the decision, that a contract by a common carrier or a contract which was designed



to hold a common carrier harmless would be void as against public policy. The Court indicates very strongly in that case that it is of that opinion and it discusses the case of *Cacey v. Virginian Railway Company*, Fourth Circuit, in considering a contract of this nature, a railroad contract, where there was no benefit given to the railroad, where they held that the railroad could enforce it, even though the railroad itself was negligent. Our Supreme Court adopted, as near as I can read the decision, the vigorous dissenting opinion by Judge Parker, who thought that the indemnity agreement did not cover personal injuries proximately caused by the railroad company's negligence. In the case of *Glens Falls Indemnity Company v. Reimers*, the Portland General Electric Company entered into a contract with Reimers and Jolivette. The contract covered some work on a building located on Southwest Second and Jefferson Street where there is a substation. The work called for in the contract was "for a complete Gunitite job." In other words, they were putting some kind of material on the exterior of a building; just what, it does not appear from the decision, [14] but I assume they were shooting it on with some kind of a gun—cement, stucco or something of that nature. At any rate, it was called the "Gunitite" process.

Under that contract the contractors agreed to hold the Portland General Electric Company harmless from all liability for personal injury, and from costs, charges or expense reasonably incurred by the

company on account of such damages, injury or claims which the PGE might sustain by anyone being injured on the job.

An employee of the contractor, while on the job and about his work, came in contact with an electric wire of strong voltage. He was up around the second or third floor of the building; I believe it was the second floor. As a result of that he received some injuries and the injured workman brought an action against the Portland General Electric Company under the Employers' Liability Act of the State of Oregon. The plaintiff recovered judgment and the Supreme Court, upon appeal, affirmed the judgment. That is where they say that violation of that act is primary negligence.

So, we submit to your Honor that it now appears in this case that the Southern Pacific Company has been found negligent under the FELA and under the instructions of the Court.

That case was submitted to the jury on the basis that if the Southern Pacific Company was negligent and also if Powers [15] was negligent he, of course, should still recover, so they either found the Southern Pacific Company's negligence was the sole proximate cause or the combined negligent acts of the Southern Pacific and of the injured man was the proximate cause, and, negligence being established and that being the negligence of the Southern Pacific, we believe we are entitled to a nonsuit. I am speaking now about the first cause of action, the first count, the first contention.

They come in and introduce a new idea. Instead of bringing their action upon the indemnity provision, they allege a breach and they say as a result of that breach, the necessary and natural result of that breach was this loss that they had. We submit that they cannot recover under the law for any breach of the contract where there is negligence causing that loss. We further submit that they could not recover for the breach, because it certainly is not in this contract that the intention of the parties is clearly manifest that the company would be entitled to indemnity for its own negligence. We submit, your Honor, under their first count, that certainly is applicable here. Furthermore, if they were allowed to recover under this first count, it would enable them to recover for their own negligence, and we think such a contract would be void as against public policy.

As pointed out by the Supreme Court of Oregon in the Reimers decision, a majority of American courts hold an indemnity [16] agreement, indemnifying against the negligence of a common carrier, would be void as against public policy.

I wish to cite *Johnson v. Richmond & D.R.R. Co.*, 11 S.E. 829-830, also *Cacey v. Virginian Railway*, decided in 1936, 85 Fed. (2d) 976-978, the dissenting opinion there being adopted by the Oregon Supreme Court, the dissenting opinion by Judge Parker.

There is a later case on that same point, *Louisville & N.R. Co. v. Atlantic Co.*, 19 S.E. (2d) 364,

decided in 1942, a Georgia case. The point appears at Pages 370 and 371, where it is held the contract will not be construed to cover loss to the indemnitee because of its own negligence unless such intention is expressed in clear and unequivocal terms.

Southern Pacific Company against Layman; Perry v. Payne, 66 Atl. 553, Page 557; North American Railway Construction Co. v. Cincinnati Traction Co., Seventh Circuit, 172 Fed. 204; and Houston & T.C.R. Co. v. Diamond Press Brick Co., 188 S.W. 32, the point being at Page 33.

In connection with the breach they refer, your Honor, to Paragraph 5 of the contract, and, in that connection, I call your attention to the fact that that paragraph is ambiguous. The fact is that this is a spur track agreement prepared by the Southern Pacific Company; it is their own language.

I call your attention to the fact that in Paragraph 5 there is this language that they are relying on: "Industry [17] agrees that without written consent of railroad first had and obtained, no structure, material, pole, cable, wire, conduit, pipe, opening, excavation or obstruction of any character, shall be erected, piled, made, stored or maintained upon or over the premises of railroad, or beneath any track upon the premises of railroad. In the event such written consent is given, industry agrees to comply with the following minimum clearances."

In that regard, your Honor, I call your attention to the fact that no obstruction shall be maintained upon or over the premises of the railroad. What







are the premises of the railroad under this agreement? The contract itself defines the term "track." I will summarize that by saying that it covers the rails, ties, switches and frogs and whatever goes in connection with that.

Therefore, "premises" would be the track and "track," as near as we can figure out, would mean to the edge of the ties. We contend there was nothing maintained on the premises of the railroad. We maintained nothing there. This cart that they have referred to, and as it appears from the record, was something on wheels that could be moved like an automobile or anything else. It does not show any breach of any of the provisions of the contract. I think you would need the written consent of the railroad if you were going onto their track to build some structure or maintain something. If you were going to do that, then you are going to be out on the track and then you must [18] apply for and get written consent, and if you apply for and get written consent, you agree that the minimum side clearance is six feet.

With respect to their second count, it reads, in effect—and appears in the bottom half of Paragraph 7,—that industry, the defendant here, would hold harmless and indemnify the railroad against any loss arising out of personal injury to its employees from an act or omission of the Booth-Kelly Lumber Company. There is nothing said in there about negligence, primary, secondary or any other kind; but if an injury occurs or results from

an act or omission of Booth-Kelly Lumber Company, then they say they are entitled to be indemnified, and here in the California case we have a direct holding that this loss occurred through an act or omission of the railroad; there was an actual omission by the railroad and, under this provision, the railroad, we submit, is not entitled to recover under this count.

Under their third proposition they say, in effect, "Regardless of the contract, we have had this loss, and you were negligent and everything; we want to be paid; we want restitution," and they claim that they are entitled to be paid some \$46,000.

To permit recovery of that nature, where it has been held that they were negligent, would be to find also that Booth-Kelly Lumber Company was, in fact, negligent; but even assuming [19] Booth-Kelly Lumber Company were negligent, one joint tort-feasor cannot collect from the other and, so, on this contract we submit, your Honor, they certainly would not be entitled to recover.

Looking at the record, your Honor, it will be seen—and I think it is quite obvious to all—that all that Booth-Kelly Lumber Company did was to create a condition. True, there was a wood cart left there. That created a condition. The railroad company was in a position—as will be seen by the Court from this transcript—to see any danger or hazard that was created by this cart. They knew it was there. The engineer knew it was there. The fireman knew it was there; the conductor knew it was there.



The brakeman, everybody knew it was there. According to this testimony, this plaintiff, Powers denied he knew it was there, but aside from him everybody else said they knew it was there.

So we submit, your Honor, that, under the evidence and under the law, the Booth-Kelly Lumber Company is entitled to a judgment of involuntary nonsuit.

The Court: Motion for involuntary nonsuit is overruled.

Mr. Powers: Pardon?

The Court: Motion for involuntary nonsuit is overruled. Have you got any evidence?

Mr. Powers: Yes, we will have some evidence, your Honor.

The Court: All right. Proceed.

Mr. Powers: We have an exception, as a matter of course, I [20] believe, to your Honor's ruling.

The Court: Yes.

Mr. Powers: First, I would like to offer our exhibits in evidence. We have here quite a voluminous transcript. It is not quite as long as it appears to be, because they don't use up the pages in full, but the pages, in double-spaced typewriting, number 370.

In this connection, is it your Honor's desire to read this or do you prefer to have us read it?

Mr. Corbett: I wonder if I might make a suggestion? About half of this testimony concerns medical testimony.

Mr. Powers: Right.

Mr. Corbett: Perhaps more than that, so that the actual amount to be read is not quite so great.

Mr. Powers: That is right. I have the medical part marked off.

The Court: Well, my suggestion is that you introduce it in evidence and let me read it.

Mr. Powers: It has already been introduced in evidence, your Honor.

The Court: Yes.

Mr. Powers: In other words, we won't have to bother about reading this?

The Court: No. As a matter of fact, I would very seriously object to your trying to read it. [21]

Mr. Powers: The defendant offers Defendant's Pre-Trial Exhibit No. 8, spur track agreement dated 1902, and, of course, Defendant's Pre-Trial Exhibit No. 9, spur track agreement dated January 4, 1909; also, Defendant's Pre-Trial Exhibit No. 10, another spur track agreement, and Defendant's Pre-Trial Exhibit No. 11, another spur track agreement, as well as Defendant's Pre-Trial Exhibit No. 12, another spur track agreement. Those are offered in evidence, and they are offered on the basis, your Honor, that they are necessary to explain the entire transaction.

Mr. Corbett: I object to them, your Honor, on the ground that they are incompetent, irrelevant and immaterial. We have in evidence the spur track agreement with which we are concerned. I see no purpose in introducing these other agreement, spur track agreements.

The Court: What are these other exhibits?

Mr. Powers: Spur track agreements that cover this same spur track since it was originally put in. We offer them to support our contention that there is no consideration for the indemnity provision contained in the 1941 agreement, and we believe that these will show that. We will offer them for the purpose of showing that this track was in operation and had been in operation for thirty-eight years.

The Court: I will permit them to go in evidence. I don't think the position is well taken because I think there is consideration in operation; there is consideration in continuing [22] operation.

Mr. Powers: Yes.

Mr. Corbett: If I may make a remark or two, I think, your Honor, the agreement of 1902, Exhibit No. 8, does not concern the track here involved, nor does Exhibit No. 12. Those concern two entirely different spur tracks. They also concern this industry, but they are distinct and apart and they have nothing to do with this transaction whatsoever.

Mr. Powers: We will endeavor to connect that up, your Honor.

The Court: All right. Put them in. The Court will strike them out if I don't see they are of any use. They are received subject to the objection.

(Spur Track Agreement, dated in 1902, was thereupon received in evidence and marked Defendant's Exhibit No. 8.)

(Spur Track Agreement, dated January 4,

1909, was thereupon received in evidence and marked Defendant's Exhibit No. 9.)

(Spur Track Agreement, dated February 27, 1909, was thereupon received in evidence and marked Defendant's Exhibit No. 10.)

(Spur Track Agreement, dated August 14, 1940, was thereupon received in evidence and marked Defendant's Exhibit No. 11.) [23]

(Spur Track Agreement, dated August 15, 1940, was thereupon received in evidence and marked Defendant's Exhibit No. 12.)

Mr. Powers: We would also like to offer in evidence at this time, your Honor, Defendant's Pre-Trial Exhibit No. 16, which is a letter written by the Southern Pacific Company to Booth-Kelly Lumber Company concerning the spur track agreement.

The Court: You entered into this agreement.

Mr. Powers: Pardon?

The Court: You entered into this agreement, did you?

Mr. Powers: The agreement signed in 1941, yes, your Honor. In this letter there is nothing said about any indemnity provision at all.

The Court: I know, but then you know perfectly well that previous negotiations do not affect the written contract. I do not have to explain that rule of law to you.

Mr. Corbett: This also concerns two spur tracks



which are not here involved. I will object to the letter on that ground.

The Court: Let me see it. If that is the size of it, I am going to reject it, of course.

This is rejected because it is something that relates to previous negotiations which are merged in the written contract.

Mr. Corbett: I will object to it on that ground, too, your Honor. [24]

The Court: I reject it.

Mr. Powers: In any event, it has been marked for identification. Perhaps it will keep out some other evidence that we have leading up to the negotiations and part of a continuing contract which had been in existence for a long time.

We will offer Defendant's Pre-Trial Exhibit 18, which is a picture that shows the boxcar caboose.

I would like to ask this of Counsel, if I may: During our pre-trial conference, when he saw this letter, I never heard him say that it was not the particular spur track we were talking about. If that is the fact, I would like to have you tell us about that, Mr. Corbett.

Mr. Corbett: I believe I mentioned in connection with Exhibit 8, certainly in connection with Exhibit No. 12, that this did not involve the spur track here involved.

Mr. Powers: You think it is a different track?

Mr. Corbett: Certainly.

Mr. Powers: Where? Could you show us here? We have got the map here now.

Mr. Corbett: Exhibit No. 12 shows on its face that it refers to a different track. In the upper right-hand corner it shows the track that was actually involved in the accident. It also refers to the 1902 agreement, which is Exhibit No. 8.

Mr. Powers: You have some agreement covering that spur where the accident occurred. [25]

Mr. Corbett: It is in evidence as Exhibit No. 1.

Mr. Powers: You do not recognize this as the same track? You don't recognize the track in Exhibit No. 1 as being the same track as that?

Mr. Corbett: They both show the same track but, if the Court please, Exhibit No. 12 shows there are two short spurs involved here, in Exhibit 12 and also in 8.

Mr. Powers: Do you think there was a separate agreement for the other track, or is it embodied in this one?

Mr. Corbett: We are bringing the action upon the spur track agreement of June 30, 1941, a copy of which is in evidence as Plaintiff's Exhibit No. 1. Exhibit No. 12, which he offers in evidence, shows two short spurs that serve an entirely different area.

I wish to renew my objection to the introduction of Defendant's Exhibit No. 8 and No. 12.

The Court: I suspect that these are all probably inadmissible. That is why I made the reservation. They are admitted subject to the objection and the Court will determine later whether they have any

validity. I have not attempted to go into this thing now. Go ahead.

Mr. Powers: We have offered the photograph. Do you have any objection to that?

Mr. Corbett: No objection; no objection to Exhibit 18.

The Court: Admitted. [26]

(Picture of side-door caboose taken February 12, 1945, thereupon received in evidence and marked Defendant's Exhibit No. 18.)

Mr. Powers: We will call Mr. Nysten.

#### ORVILLE A. NYSTEN

was thereupon produced as a witness on behalf of Defendant and, being first duly sworn, was examined and testified as follows:

#### Direct Examination

By Mr. Powers:

Q. Your name is Orville A. Nysten?

A. Yes.

Q. Where do you live, Mr. Nysten?

A. Springfield, Oregon.

Q. Are you employed by the defendant?

A. I am.

Q. What is your work with the defendant?

A. Well, at the time of the accident, at the time the accident occurred I was superintendent.

Q. Superintendent?

A. Of the Booth-Kelly Lumber Company, yes.

(Testimony of Orville A. Nysten.)

Q. You were superintendent of the mill property, were you?           A. Yes.

Q. What is your position now? [27]

A. Assistant superintendent.

Q. How long have you been employed at that property for the Booth-Kelly Lumber Company?

A. I commenced work the first day of April, 1911; continuous employment ever since; that is about, just about 38 or 37½.

Q. 37½ or 38 years?           A. 37½ years.

Q. How many spur tracks do you have into the property?

A. Well, we got two loading tracks, where we load lumber, and then we got this logging track or spur where we push the logs up to the log pond.

Q. The logging track, is that where the accident occurred we are talking about?

A. That is right.

Q. How long has that logging track been in there?

A. It was there before I came there.

Mr. Corbett: Object to that as immaterial.

The Court: He has answered.

Mr. Corbett: I move that the answer be stricken.

The Court: Denied.

Q. (By Mr. Powers): You examined the blueprint attached to the track agreement, did you not?

A. I have, yes.

Q. Did you find the logging track that we are speaking of on both of those blueprints? [28]



(Testimony of Orville A. Nysten.)

A. Well, I think the logging——

Q. I will hand you Defendant's Exhibit No. 12, which is the agreement dated August 15, 1940, and ask you to examine that and see if you can find the line indicating the spur track on which this accident occurred?

Mr. Corbett: I will object to that, if your Honor please. I believe from this contract it can be seen what track is covered by it. If the agreement does not cover the spur track here involved, then that agreement is immaterial as far as this action is concerned. The fact that the agreement might have a map attached which also showed other tracks would have no bearing that I can see in this case.

The Court: Well, I don't know what his theory is.

Mr. Corbett: I beg your pardon.

Mr. Powers: Well, your Honor, my theory is that the first contract that they had covered this spur track that we are talking about in 1902, and it covered tracks in the mill and woods, all the way through. This spur track was put in under agreement made with the railroad company back in 1902 and this same track has been there all that time, I think, on both of these blueprints, that it is the track referred to in the 1902 agreement.

The Court: What difference does it make?

Mr. Powers: Well, your Honor, of course our evidence is going to disclose this as we go along, but

(Testimony of Orville A. Nysten.)

it makes a difference, [29] we believe, to show that there was no consideration here.

The Court: I do not see how it can be possible that there could be no consideration, when you signed the agreement to operate this and haul your product over this spur track. I don't see why it makes any difference whether you had an agreement of this type or not.

Mr. Powers: Well, under the decisions that I have read we felt that it did have something to do with it. Our evidence will disclose here they were hauling our logs; that this agreement gives them the right to use the track for any kind of business they want to use it for; that they are using this piece of track and they have been for the past several years, and while this was going on, not in connection with the business of the Booth-Kelly Lumber Company, but they were hauling logs for the Springfield Plywood Company; they hauled logs almost day in and day out across this track to the Springfield Plywood Company, not for the Booth-Kelly Lumber Company, because they have the right under this agreement to use it for their own purposes. They haul shingles for the Huntington Shingle Company, and they lease some of their property, Southern Pacific property, where this particular track is located. The Booth-Kelly Lumber Company does not own it. The Booth-Kelly Lumber Company does not own the property where this occurred, but it is leased from the Southern

(Testimony of Orville A. Nysten.)

Pacific to Booth-Kelly, for them to use it, I think for \$70 a year or so. [30]

What I thought about this letter was, since the spur track has been in there for such a long period of time—And Mr. Nysten was going to testify that the track was in long before this 1940 agreement was signed—that it did not add anything else as far as that track was concerned; that they had to serve industry and that they had no right to insist, without any consideration, that they put in the indemnity provision. It is our contention they are common carriers and their duty is set forth, I believe, by a statute, and we would have a right to insist that they serve us, since we entered into an agreement which was still in effect—no consideration for canceling it—and presented another agreement to Booth-Kelly under the pretext that it was to show ownership and thereupon changed that ownership in the track. We think it has a very definite place in the case.

Inasmuch as the Court has taken up this question of consideration, we felt we should show the entire transaction. By this letter we have not offered or attempted to show anything that preceded this agreement, but we are trying to show the series of transactions that started from the first contract and continued on up to the time the accident occurred. This letter is only part of that series.

Mr. Corbett: If the Court please——

Mr. Powers: Excuse me. I might say that the agreement of 1941, I believe, refers to the agree-

(Testimony of Orville A. Nysten.)

ment back in January, January 4, 1919. [31]

Mr. Corbett: But not to the agreement in 1902 nor to the agreement signed August 15, 1940. Those are entirely different tracks.

The Court: Go ahead. I will receive the evidence. I do not want to hear a lot of argument about it. I don't think it has anything to do with it; I will tell you that right now.

Q. (By Mr. Powers): You went to work for Booth-Kelley Lumber Company about what date?

A. April, 1911.

Q. 1911? A. Yes.

Q. This spur track where the accident occurred was in there at that time?

A. Yes. That was the only way we had to bring logs into the company at that time.

Q. You used to bring logs in on railroad cars, that is, Booth-Kelley; isn't that a fact?

A. That is right.

Q. Where did those logs come from?

A. They came from Wendling.

Q. Has Booth-Kelley discontinued bringing logs in over that spur track?

A. Well, yes, they bring them in by trucks now.

Q. When did you stop your logging at Wendling? When did you stop bringing logs from Wendling? [32]

A. I don't know just the date but I imagine right around ten years, I imagine, or better since we quit that.



(Testimony of Orville A. Nysten.)

Q. Then you started hauling in by truck, is that right?      A. That is right, by trucks.

Q. Do you have logs coming in over that spur track occasionally or on rare occasions now?

A. Oh, it might be possible. I wouldn't say we haven't had some, but there is very few cars for Booth-Kelly's own use.

Q. Whose logs come in over that track?

A. Springfield Plywood and Huntington Shingle Mills, some, but not all of them.

Q. The railroad uses this same spur track where the accident occurred for bringing in logs for the Springfield Plywood and the Huntington Shingle Mill?      A. Yes.

Q. Where is the Huntington Shingle Mill located with respect to where the accident occurred? Is it towards the main line or is it away from the main line of the railroad?

A. It is away from the main line.

Q. The Huntington Shingle Mill—Are the dry kilns of that mill located on Southern Pacific property?      A. Yes.

Mr. Corbett: I object to that, your Honor. I do not see the materiality of this particular question.

The Court: I am frank to say I do not see what any of it [33] has to do with the case.

Mr. Corbett: I would like a blanket objection to this whole line of testimony.

The Court: No. I won't do that. I will overrule the objection. As I say, I think it is very doubtful

(Testimony of Orville A. Nysten.)

that it has any place in the case, but I will listen to the evidence.

Q. (By Mr. Powers): Did you go out to the scene of the accident after it occurred that day?

A. Yes, I did.

Q. The logs that were brought in that particular day, were they coming in for Booth-Kelly or someone else?

Mr. Corbett: Object to that, your Honor, on the ground that the defense of the case of Powers vs. Southern Pacific having been tendered to Booth-Kelly, they are estopped from going back of the facts as there determined.

The Court: Objection overruled.

Q. (By Mr. Powers): To whom did the logs belong that Southern Pacific brought in the day that the accident occurred?

A. Springfield Plywood Company.

Q. Can you tell the Court something about the woodcart that was there at that time, Mr. Nysten?

The Court: Isn't this all in the testimony, one way or another, set forth in the pre-trial order?

Mr. Powers: Yes.

Mr. Corbett: I would like to object to that question, your [34] Honor, as incompetent, irrelevant and immaterial. It covers a fact already determined by the pre-trial order.

Mr. Powers: We could not give you a good description, I thought, after ten years, by a photograph of what the thing looked like. It is not of

(Testimony of Orville A. Nysten.)

any particular consequence except I wanted to show the Court what it was and how it happened to be there. There is nothing in that to show how it happened to be there at the time when it was left there by the defendant.

The Court: Well, I don't see what you are talking about, but you go ahead on your own theory. I think this is all irrelevant and immaterial.

Mr. Corbett: My objection is overruled?

The Court: Yes, objection overruled.

Q. (By Mr. Powers): What is the cart used for that was there at that time?

A. It is to haul wood, a woodcart, I think.

Q. What is the wood used for?

A. For locomotive cranes.

Q. Where are the carts filled up?

A. At the plant.

Q. That is, over at the sawmill?

A. The Booth-Kelly plant.

Q. How do you get them out to the cranes?

A. Pulled over by a tractor or jitney.

Q. This particular area where the woodcart is located, is [35] there a road for vehicular travel right along there?      A. Yes.

Q. Did you have any knowledge, any personal knowledge, that this cart was there before the accident, had been left that close to the track?

Mr. Corbett: Object to that, your Honor. It is admitted it was placed and left there by the defend-

(Testimony of Orville A. Nysten.)

ant. I think this is all immaterial, incompetent and irrelevant.

The Court: Objection overruled.

Q. (By Mr. Powers): Did you have any personal knowledge that the cart was there?

A. I know one of the fellows come and asked for wood to be brought up there but I didn't see the cart actually pulled over to the track, but that particular cart was standing there for a few days, I know. Nobody made any objection to it. In fact, I really thought it was in proper clearance of the track, but I guess it wasn't.

Q. You don't remember how close it was to the rail, is that it?

A. I didn't, not before the accident.

Q. Mr. Nysten, this area where the accident occurred—Going back to the time that the accident occurred—were there numerous employees of Booth-Kelly around there?      A. No.

Q. Was it a remote place, or otherwise?

A. People would go by there, but not very often. [36]

Q. What employees of Booth-Kelly were working around there, any where close around there?

A. Nobody working right there at that particular place; that is, right where that cart was sitting.

Q. How close to the cranes that you are speaking about was that kindling?

A. I imagine about a couple of thousand feet



(Testimony of Orville A. Nysten.)

or better; maybe more than that from that place.  
I don't just quite——

Q. Over this long period of years that it has been there do you ever remember any occasion when there would be impaired clearance?

A. As I have been notified, yes.

Mr. Corbett: I object to that as not responsive.

The Court: Objection sustained. Stricken.

Q. (By Mr. Powers): Over that period of years you have had some dealings with the railroad company with respect to their switching operations?

Mr. Corbett: That is objected to, your Honor.

The Court: It is not going to hurt. I can get his answer without being prejudiced.

Q. (By Mr. Powers): Did you answer?

A. No, I didn't answer. What was the question?

Q. Well, I will reframe it. When any negotiations were carried on by the railroad employees with the Booth-Kelly mill with respect to obstructions on the track, clearances and so forth, how were they carried on? [37]

Mr. Corbett: I object to that as immaterial, and object to this whole line of testimony on the ground that he is seeking to vary a written document by parole evidence.

The Court: Objection overruled.

Q. (By Mr. Powers): How were they carried on? . A. Oh, with me.

(Testimony of Orville A. Nysten.)

Q. They carried on those negotiations with you?

A. Yes.

Q. Was there a course of procedure or a custom and practice there with respect to having obstructions removed where the clearance was impaired?

Mr. Corbett: Objected to as calling for a conclusion of the witness, also seeking to obtain testimony that would vary a written contract. Objected to on the further ground that the answer, if given, would be irrelevant since the witness has admitted now the presence of the cart and, furthermore, it is admitted in the pre-trial order that the defendant knew of the presence of the cart by reason of the fact that they placed it there, so this evidence would be immaterial.

The Court: Objection sustained.

Mr. Powers: We are offering it for a little different reason, your Honor. The point is raised in the pre-trial order whether there was a custom and practice here and an interpretation placed on the contract by the parties themselves with respect to any obstructions or any impairment of clearance, and [38] it was to that end that we sought to develop——

The Court: Just a moment. I have already ruled. Just let it go at that. Objection sustained.

Mr. Powers: All right, your Honor.

Q. After this spur track was in there, were there any extensions to the spur track near where the accident occurred?

(Testimony of Orville A. Nysten.)

A. Not where the accident occurred, no.

Q. Remained the same all the time you were there, from 1911 down to date?

A. It might have been added to at the other end, about a half-mile or a mile further down.

Q. Did the railroad company, with respect to this particular date when the accident occurred, when the cart was there, ever give you notice that it was impairing the clearance, or to move it?

Mr. Corbett: Objected to as incompetent, irrelevant and immaterial. The cart was placed there by Booth-Kelly Lumber Company. Notice would not be material in any event since the Booth-Kelly Lumber Company is presumed to know its own actions.

The Court: Objection overruled.

Q. (By Mr. Powers): Did they give you any notice about moving it or make any complaint of impaired clearance? A. No.

Q. You have seen the converted boxcar that was used as a caboose, have you? [39]

A. Yes.

Q. Can you tell the Court the difference between an ordinary caboose and that boxcar, as far as a person descending therefrom is concerned?

Mr. Corbett: I believe that is already covered in the testimony in the case and I will object to it as being irrelevant, your Honor.

The Court: Objection overruled.

Q. (By Mr. Powers): Would you tell the Court, please?

(Testimony of Orville A. Nysten.)

A. Well, a converted boxcar is a car that hasn't got regular steps on the front and back end of it; just a door, which has handbars;—What the S.P. Company call them I don't know—I don't know what they call these, but that is the difference. A caboose has regular steps and railings and you don't have—In other words, you don't have to back out of it to go down from the front end, either the front end or back end.

Q. You do not have to back out of the regular caboose?      A. No.

Q. Out of this converted caboose, do you have to back out?      A. Have to back out.

Q. Are the steps on the regular caboose back out of the line of the train? In other words, do they stick out beyond the side of the car?

A. The regular caboose has regular steps right down. They don't stick outside, no.

Q. They do not? [40]      A. No.

Q. In getting out of this converted boxcar—

A. Well, I really have—I haven't really examined it real close, but I think it is right under the boxcar, myself, the steps.

Q. Over your long period of time there as superintendent and as an employee, do you know about the way in which the railroad company operates its trains, the rules and regulations for operating and for flagmen and brakemen?

Mr. Corbett: Object to that as immaterial. I



(Testimony of Orville A. Nysten.)

don't know—I don't see how that has any bearing on this case.

The Court: Objection sustained.

Mr. Powers: I believe that is all, your Honor. Could we make an offer of proof?

The Court: Oh, yes. Dictate it into the record. You may dictate it in the record after court.

Mr. Powers: Yes, your Honor.

The Court: The Court is going to recess now until tomorrow morning at 10:00 o'clock.

Mr. Corbett: Has Counsel rested his case?

Mr. Powers: No.

#### Defendant's Offer of Proof

Mr. Powers: If the Witness Nysten had been allowed to answer the questions with respect to which the Court sustained plaintiff's objections, he would have testified that there had [41] been a course of conduct in dealings between the parties whereby when any obstruction or impairment of the clearance existed, which the railroad company felt needed to be removed, that the railroad company, through its employees,—sometimes the train crew and sometimes the freight or station agent—would notify this witness or other employees of the Booth-Kelly Lumber Company and they invariably would remove the obstruction immediately; that on numerous occasions there have been loads of lumber on push trucks, there have been carts, automobile trucks and automobiles that were as

close or closer than this particular wood cart from the nearest rail, and these obstructions, when called to the attention of the Booth-Kelly Lumber Company, would always be removed and removed immediately.

This witness would further testify that he did not say that he had personal knowledge that this wood cart was located within forty-two inches of the nearest rail, as stated by plaintiff's counsel, but, on the contrary, he stated that he knew that the wood cart was up there but did not know that it interfered with the clearance; if he were allowed to clear this matter up, that is what he would testify to, which evidence was kept out by objection of plaintiff's counsel. [42]

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Friday, November 12, 1948, hearing of the above-entitled cause was resumed pursuant to adjournment.

The Court: I have decided, Mr. Powers, to let you put in all the evidence you think is competent, subject to objection.

Mr. Powers: Thank you, your Honor.

The Court: Even though I think right now that this matter, although mentioned in the pre-trial order—I think this matter of custom, at least in that form, is not pertinent but, in any event, in order to be sure that you have opportunity to present your theories, the evidence will be received, subject to the objection, with the idea even-

tually, upon consideration of the case, that I will strike it out if I think it should be stricken.

### ORVILLE A. NYSTEN

having been previously duly sworn, thereupon was recalled as a witness on behalf of Defendant, and was examined and testified as follows:

#### Direct Examination

Mr. Corbett: Before we commence, your Honor, if this relates to testimony that was previously stricken, it won't be necessary for me to renew my objections to each question, will it?

The Court: I think you had better renew your objection when the evidence comes in. I say that because—It doesn't make any difference to me—these appellate courts act under this rule that says if there is any issue to try which is not objected to [43] that they can decide the case on that, without anything further, and I think, if you are going to protect your record, you should make proper objections. I would not consider it at all if I thought it was not a proper issue, but some appellate court might say that you consented, so you had better protect your record and state your objections when you think they should properly be made.

Mr. Corbett: Thank you, your Honor.

Q. (By Mr. Powers): Mr. Nysten, over the period of years while you were superintendent, and

(Testimony of Orville A. Nysten.)

with respect to the spur track of the Booth-Kelly Lumber Company, was there a custom or practice developed as to the removal of any obstructions to the clearance between the Booth-Kelly Lumber Company and the railroad?

Mr. Corbett: I will object to that, your Honor.

A. Our traffic——

Mr. Corbett: I will object to that on the ground it is incompetent, irrelevant and immaterial and on the ground that it is an attempt to vary the terms of a written instrument; it is irrelevant since it would have to do with giving notice of a condition which was placed there in this particular case by the defendant, and that there would be no authority on the part of the defendant to create such a variation of a written contract.

The Court: The testimony will be received at the present time, subject to the objection. The objection is overruled. [44]

Q. (By Mr. Powers): Will you answer the question, Mr. Nysten?      A. Yes.

Q. And what was the practice when there was an obstruction to the rail clearance?

A. Well,——

Mr. Corbett: The same objection, your Honor.  
The Court: The same ruling.

A. We always cleared it.

Q. (By Mr. Powers): And who would notify you to clear it?

Mr. Corbett: The same objection.



(Testimony of Orville A. Nysten.)

The Court: The same ruling.

A. Generally the agent or brakeman, and so on, whoever noticed the obstruction.

Q. (By Mr. Powers): When you speak of the agent, which agent do you refer to?

Mr. Corbett: The same objection, your Honor.

The Court: The same ruling.

A. At the station there, the depot agent.

The Court: What is the name?

A. Allen.

The Court: What are the names of these other people?

A. Well, I don't know the brakeman.

Q. (By Mr. Powers): The various members of the train crews?

A. No, I don't know them.

Mr. Corbett: The same objection. [45]

The Court: The same ruling. Besides, I would suggest you had better let the witness testify.

Mr. Powers: Yes.

Q. When you say the brakeman would tell you, the brakeman of what?

Mr. Corbett: The same objection.

The Court: The same ruling.

A. Sometimes might be something in their way, maybe, that I didn't think really was safe, but not very often that happened.

Q. (By Mr. Powers): What kind of obstructions would that be?

Mr. Corbett: The same objection.

(Testimony of Orville A. Nysten.)

The Court: The same ruling.

A. Well, that varies; something dropping off a truck of maybe a stick of lumber, you know, by moving lumber and stuff like that, you see, would be turned around and be close to the track, but we watched that pretty thoroughly ourselves, but it is possible, you know, around a plant——

Mr. Corbett: Object to that and move that it be stricken as not responsive.

The Court: The same ruling. Motion denied.

Q. (By Mr. Powers): Mr. Nysten, with respect to the point where this accident occurred, could you make a mark on the blueprint which we have in evidence, showing where the accident occurred? It is a plaintiff's exhibit.

Mr. Corbett: Object to that, your Honor. That is determined [46] in the previous case of Powers against the Southern Pacific, and I object to that unless the Court desires to have it done.

Mr. Powers: That is the only reason I am doing it, your Honor. You might wade through that entire transcript and finally locate it, but we have a plat here——

The Court: All right.

Mr. Powers: If we could have him mark it, it would simplify it.

The Court: Objection overruled.

Mr. Powers: Hand the witness Plaintiff's Exhibit No. 1.

(Plaintiff's Exhibit No. 1 handed to the witness.)

(Testimony of Orville A. Nysten.)

Q. (By Mr. Powers): Attached at the bottom you will find a blueprint, I believe. Are you able to find the location where the accident occurred on the blueprint? A. Yes.

The Court: Step down to the table and do that.

Q. (By Mr. Powers): Make an "X" mark, if you please, here where the accident occurred, if you find the point where the cart was located at the time the accident occurred.

A. (Witness illustrates as instructed.)

The Court: This is in red, that line pointing to the spot, that spot, is that right?

A. Yes.

Q. (By Mr. Powers): That mark that you have made on the exhibit, Mr. Nysten, as to where the accident occurred, what distance is [47] that from the railroad station, in a direct line?

A. Oh, I wouldn't think it is over about 150 or 200 feet, not over that, I don't believe; about 200 feet, I imagine.

Q. The mark you have made with the red pencil, that is somewhat lighter than these other lines.

A. With the red pencil, yes.

Q. Over near the circle that is marked "W.C."?

A. Yes.

Q. What is that "W.C."?

A. That is "Wood Cart."

Q. Then there is a mark on this blueprint "W.T." out there. It is kind of a circle. Do you know what that is? A. "W.T." in a circle?

(Testimony of Orville A. Nysten.)

Q. Yes.

The Court: I think I know.

Mr. Powers: All right. I thought I did, too, but I didn't want to make any suggestions.

The Court: All right. You can ask him.

Q. (By Mr. Powers): Is there any place there for them to water their engines? That "W.T." with a circle around, what is that?

A. That is for the water tank.

Q. The water tank? A. Yes.

Q. The property where the accident occurred, is that owned by the Booth-Kelly Lumber Company, or do you know? [48]

Mr. Corbett: Object to that as immaterial.

The Court: Objection overruled for the present. You may answer.

A. Well, I really believe that is S.P. Company's property.

Mr. Powers: While it is the S.P. property, the Booth-Kelly Lumber Company leases the area out there, does it not? A. That is right.

Q. For about \$70 a year?

A. Well, I don't know what they pay, but they lease the land on that track there (indicating).

Q. In the general vicinity where the cart was located is there a roadway?

A. That is right. There is a regular roadway up there.

Q. The spur track which we call the logging track, does the railroad use that track for anything other than you mentioned yesterday?



(Testimony of Orville A. Nysten.)

A. They use it sometimes—It was the practice when they pull in to shove the caboose up there so they would have more room to switch. It is pretty crowded for room there anyway, I believe, for switching facilities.

Q. The Huntington Shingle Mill you referred to yesterday, is freight from there moved over this logging spur?      A. That is right.

Mr. Corbett: Object to that as immaterial.

The Court: Objection overruled. [49]

Mr. Corbett: Incompetent, irrelevant and immaterial.

The Court: Objection overruled for the present.

Q. (By Mr. Powers): Is part of the Huntington Shingle Mill located on the property owned by the Southern Pacific?

A. Part of the property is.

Mr. Corbett: Objected to as immaterial.

The Court: He may answer.

Q. (By Mr. Powers): You have looked at the blueprint, Mr. Nysten, the one attached to Plaintiff's Exhibit No. 1 and also to the blueprint attached to Defendant's Exhibit No. 12.

A. I don't believe I have seen the blueprint of 12.

Q. Do you see the lines indicating the spur track you have been testifying about on both blueprints?      A. Yes.

Mr. Corbett: Object to that testimony as incompetent, irrelevant and immaterial. These docu-

(Testimony of Orville A. Nysten.)

ments speak for themselves. I don't think oral testimony would add anything to them.

The Court: The objection is overruled for the present.

Q. (By Mr. Powers): What is your answer?

A. I said the same drawings, except that there are two more tracks on it.

Q. The spur track you have been talking about, that has been in the same location, the same place, ever since you went there in 1911?

A. That is right, ever since I worked there.

Mr. Powers: I believe that is all, your Honor.

The Court: The Court gives you the right to cross-examine now, without waiving your objections.

Mr. Corbett: Very well, your Honor.

Mr. Powers: Perhaps I should put in some exhibits that I did not get offered yesterday. Defendant's Exhibit No. 14, marked at pre-trial, is a copy of the general safety rules of the Southern Pacific. We will offer that in evidence.

Mr. Corbett: I will object to the introduction of the rules as incompetent, irrelevant and immaterial. I believe there is some mention of the rules, some specific rules, in the Powers case and as to those, of course, I would have no objection, since they are already in the record.

The Court: It will be received, subject to the objection.

(Testimony of Orville A. Nysten.)

(Copy of General Safety Rules, Southern Pacific Company, thereupon received in evidence and marked Defendant's Exhibit No. 14.)

Mr. Powers: The defendant would also like to offer in evidence Pre-Trial Exhibit No. 15, marked for identification. It is a copy of the rules and regulations for the maintenance of way of the Southern Pacific Company. I might say, your Honor, these rules were furnished to us by the Southern Pacific.

Mr. Corbett: The same objection, your Honor.

The Court: Objection overruled for the present. The exhibit is received, subject to objection. [51]

(Copy of Rules and Regulations, Maintenance of Way, Southern Pacific Company, thereupon received in evidence and marked Defendant's Exhibit No. 15.)

Mr. Powers: We would like to offer in evidence, your Honor, Defendant's Pre-Trial Exhibit No. 17, which is a letter dated February 5, 1940, written by the Southern Pacific Company to the Booth-Kelly Lumber Company.

The Court: I will stand on my ruling on that.

Mr. Corbett: I will object to it, your Honor.

The Court: I don't think that has anything to do with the situation, if that is the same letter you offered.

Mr. Powers: It is not the same letter, but it

(Testimony of Orville A. Nysten.)

goes to the same matter, your Honor. I merely offer it to show what was going on at the time that contract was entered into.

Mr. Corbett: This is dated in February and the agreement was signed—This was dated in February, 1940, and the agreement was signed in June of 1941.

The Court: Rejected.

Mr. Corbett: I have no cross-examination, your Honor.

(Witness excused.)

Mr. Powers: I am going to ask Counsel to stipulate about one answer which they gave us, if the matter becomes an issue in the case as to the combined negligence or proximate cause. [52] There is one allegation that the railroad was negligent in not having any signs posted on the boxcar telling anybody in getting out of there that they should first look, and that they have got to go out backwards. We are asking Counsel to stipulate that there were no signs posted in or on the caboose covering the manner of detraining.

Mr. Corbett: I am not sure as to whether that is in the pre-trial order. I think a contention is made as to that that states the fact correctly, your Honor, but I am not sure whether that would require an amendment of the pre-trial order or how that would be handled.

Mr. Powers: The pre-trial contention is that the railroad company failed to put a sign in the



converted caboose warning trainmen of the danger descending therefrom in a backward manner without first looking to see the way was clear.

Mr. Corbett: That is correct. There is a statement made in the answer to the interrogatory.

The Court: Read it into the record.

Mr. Powers: "No signs were posted in or on the caboose regarding the manner of detraining." It is so stipulated.

Mr. Corbett: Yes.

The Court: I suppose it is objected to on account of materiality?

Mr. Corbett: Yes, your Honor. I would object to it on that ground, although it states the fact correctly. [53]

The Court: Objection overruled for the present.

Mr. Powers: That is our defense, your Honor. The rest would be merely cumulative.

Mr. Corbett: With regard to the testimony as to custom, would it be permissible for me, without waiving my objection, to put on a rebuttal witness?

The Court: Yes.

Mr. Corbett: In regard to that testimony?

The Court: Yes.

Mr. Corbett: May I ask a short recess? I want to have Mr. McColloch called as a witness as to that, and he could be here in a short time, I am sure.

The Court: Yes. I will permit that. Have you any objection?

Mr. Powers: No objection, your Honor, at all. If it would save any time, I could make a motion now or I could make it after they get their evidence in.

Mr. Corbett: That would not change the legal points at all going to the rest of the motion for a directed verdict.

The Court: Could you stipulate as to what Mr. McColloch would testify to?

Mr. Powers: Have you in mind what that is?

Mr. Corbett: Yes.

Mr. Powers: Go ahead and state what he would testify to.

Mr. Corbett: Mr. McColloch, if called as a witness, as a [54] rebuttal witness, with regard to this matter of custom, would testify that the only employee of the Southern Pacific Company in the State of Oregon who would have authority to sign leases and similar agreements would be the superintendent and——

The Court: What is his name?

Mr. Corbett: In this case I believe Mr. E. L. King was superintendent at the time this agreement was signed; that he would only enter into such agreements after approval from the management in San Francisco; and that, in cases of industrial track agreements, or in some cases of industrial track agreements, the whole matter

would have to be approved by the executive committee of the company.

There is one exception to that and that would be the General Agent in Oregon who, at that time, would have been Alfred A. Hampson.

This testimony would go to the lack of authority on the part of employees to establish any such a custom.

The Court: Who is Mr. McColloch?

Mr. Corbett: Mr. Frank T. McColloch is the statutory agent and attorney-in-fact and general agent for the Southern Pacific Company in Oregon at the present time.

The Court: Does he have actual knowledge of the things about which he would testify?

Mr. Corbett: He would have actual knowledge of the authority. Will you stipulate as to that testimony? [55]

Mr. Powers: I will stipulate that if he were called he would testify to that effect.

Mr. Corbett: It is understood that testimony, your Honor, is going in under that stipulation, that we are not waiving any objections we may have as to that testimony as to custom.

The Court: The Court will so direct. Mr. Powers, I assume you think that is not material and you will be allowed an exception to that.

Mr. Powers: Yes, your Honor. Thank you.

Mr. Corbett: The plaintiff rests.

## Defendant's Motion for Directed Verdict

Mr. Powers: At this time, if the Court please, the defendant moves the Court for a directed verdict on the ground that it appears under the law that they are not entitled to recover on any of their counts.

It appears from the evidence that they have submitted and under the stipulation the primary cause or loss was the railroad company's own negligence, and that a common carrier cannot recover under such a contract if it is a loss suffered through its own negligence or, for that matter, the negligence of the company combined with that of anyone else. We also would like to incorporate the same grounds mentioned in connection with the motion for nonsuit, just to save time.

The Court: Yes. [56]

Mr. Powers: We have this additional contention at this time, your Honor, that it now appears in the record that at the time the accident occurred the logs being moved were being moved for the Springfield Plywood Company and not for the Booth-Kelley Lumber Company, and under the interpretation which I think would be placed on the contract, in any event, there is certainly nothing in the agreement which makes it manifestly clear that the intention was that where the railroad company was doing something for its own benefit, operating as a common carrier, hauling other people's freight, that this defendant would not be required to indemnify the railroad. I call your



Honor's attention to the fact that in this agreement the railroad company, starting with the earliest agreement, consistently reserved to itself the right to use this track in its own business and that is what it was doing here.

As to the last count in which they seek to recover on the basis that maybe both the parties were negligent here, we submit they are barred from recovery on the basis that one tort-feasor cannot recover from the other, under the laws of Oregon.

The Court: The motion is for directed verdict—That does not quite describe it, because when a Court is trying a case without a jury there is no such a motion, I take it, but it would be for judgment as a matter of law. It is denied. The Court is going to decide this case on the facts. The [57] facts have all been presented. There is no reason for ruling on the question of law. The Court will determine what the facts are and thereupon decide the law in relation to the facts.

I think there is quite a serious question in this case. I think both sides had better brief it. That is my notion about it.

I will give you some light on the question. I think the question is serious because of the fact that the Southern Pacific Company was not subjected to liability because of the condition itself or negligence in leaving the obstruction there. The groundwork apparently was the liability which was imposed upon the Southern Pacific Company by a failure to warn which seems to take it out of the

category of things for which it can ask for indemnity but, on the other hand, the contract is fairly specific with respect to what Booth-Kelley Lumber Company did, indemnifying itself against all liability for any accident; but, as regards failure of consideration, I do not think that business corporations enter into this kind of a contract without knowing what they are doing, and I think that the Booth-Kelley Lumber Company certainly thought that there was some consideration or they would not have done it and, so, I don't know why I should be wiser than the contracting parties. Business corporations usually have fairly competent legal advice. In this instance I suspect that they both had it and so, therefore, in a contract which is as specific as this one is, and where [59] various clauses are stricken out of the form and various clauses are added on top of the form, I am of the opinion that they knew what they were doing in the first place, and that they had legal advice on the subject, and at least both sides thought there was a consideration, and it would be very difficult for me to make a finding of lack of consideration, but I will still keep an open mind on it, if counsel can convince me on the subject. I would be glad to hear any arguments that counsel may wish to present, in briefs. I really think that is one of the things that a Court is not supposed to know, that business corporations usually act advisedly. This Court happens to know, and, so,

you won't spend too much time in arguing that they did not know what they were doing.

I still say on the other feature I think there is a very serious question. I think it is a very close question and I would appreciate all the light I can get from counsel. How much time do you wish to have? Mr. Corbett, I assume you will have the burden.

Mr. Corbett: If twenty days would be agreeable to the Court——

The Court: I do not care how much time you take. I shall give you whatever time you suggest.

Mr. Corbett: Then I might suggest thirty days, and I will try to get my brief in before that time, if that is possible. [59]

The Court: All right; thirty days to each side, and five days to you to reply.

Mr. Corbett: I would like to suggest that I file the opening brief, that Mr. Powers file the answering brief explaining his contention, and then that I be allowed time to file a reply. I am not saying I would be able to answer in five days, your Honor. I would rather have a shorter time to open and add that time for replying.

The Court: All right. I will give you ten days.

Mr. Corbett: Very well.

The Court: Thirty, thirty and ten. Anything else, Gentlemen?

Mr. Powers: I believe that is all, your Honor.

The Court: The Court is in recess. [60]

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United States District Court  
District of Oregon

No. Civil 3989

SOUTHERN PACIFIC COMPANY,  
a Corporation,

Plaintiff,

vs.

THE BOOTH-KELLY LUMBER COMPANY,  
a Corporation,

Defendant.

Before: Honorable James Alger Fee,  
Judge.

June 13, 1949

DECISION OF THE COURT

The Court: Southern Pacific Company, a corporation, Plaintiff, against The Booth-Kelly Lumber Company, Defendant, Civil 3989.

This is an action brought by the Southern Pacific Company on account of the loss sustained by that company as plaintiff as a result of an accident which happened upon the spur track operated partially for the convenience of The Booth-Kelly Lumber Company. The matter arises under a written contract between the plaintiff and defendant.



The Southern Pacific Company was sued in California for the injury, and Powers, the plaintiff there, recovered a substantial judgment.

The question presented to this Court is as to whether there can be a recovery by the Southern Pacific Company upon the contract with The Booth-Kelly Lumber Company, and the Court rules that there can be. In view of the fact that its interests were served by the making of this contract, and in view of the fact that the accident would not have happened if it had not been for an act of defendant which an ordinarily prudent person would not have done, it is just and in accordance with its contract that it should pay the loss. However, since the railroad was in some measure also at fault which contributed to the accident, judgment is given under the contract for only one-half of the damage.

The Court has tried the question of damage on the transcript introduced in evidence in this case. However, the Court did not treat the finding as binding in any respect, using it simply as advisory under the transcript.

The Court therefore will make findings in accordance with the requests which were set out in the pre-trial order, as follows:

#### Issues of Fact

1. Was the damage to Powers and the liability of plaintiff the natural or necessary result of defendant's breach of contract?

Yes.

If so, in what amount?

\$44,000.00.

2. Was plaintiff damaged by reason of an act or omission of the defendant, its agents or employees, to an employee of plaintiff while on the industrial track?

Yes.

If so, in what amount?

The actual loss of plaintiff, the amount of the judgment, and the amount of legal fees and costs involved in this action. This was the loss. The question of whether it was legal damage or not is another matter, and is answered in the first question.

3. Was defendant negligent in placing and leaving the wood cart within 42 inches from the track?

Yes.

4. If so, was defendant's negligence in this regard the active or primary cause of the injury to plaintiff's employee, Powers?

Yes.

5. Did the damage to plaintiff's employee arise from the joint or concurring negligence of plaintiff and defendant?

Yes, the direct, proximate and primary cause of the injury being the negligence of defendant, but with some elements which concurred to cause the accident on the part of the plaintiff. Powers vs. Southern Pacific was between different parties and is not treated as res adjudicata here. The Court,

however, did consider the amount of the verdict as a fair appraisal of the damage to Powers.

6. In the matter of the railroad company's negligence as determined in the California proceeding and trial *res adjudicata*?

No.

If not, was the railroad company negligent in any of the particulars specified in the defendant's contentions?

The Court considers the acts or omissions of the employees of plaintiff contributed to the injury of Powers, but not in the form of the specifications of the defendant.

7. Was the negligence of Booth-Kelly, if any, remote?

No.

8. Was there any consideration for the indemnity provision in the track agreement?

Yes.

9. Is plaintiff barred from recovering under the track agreement by reason of its own acts and conduct?

No.

10. Was there a custom or practice between the parties under which the plaintiff would give notice to defendant of any objectionable obstruction to track clearance, and a further custom of defendant removing the same at the request of the railroad?

No. Any acts of this sort upon the part of the

railway employees would simply be in an attempt to maintain a safe operation. No matter how many times such incidents occurred these incidents would not ripen into a custom. It was simply an attempt to keep a safe operation of the railroad.

11. Did the plaintiff discover the alleged breach prior to the accident; and, if so, was the loss and damage caused by plaintiff's conduct in continuing operations without taking steps to have the cart removed or to warn its employees thereof?

Some of the employees of plaintiff observed the position of the cart, and operations and work continued thereafter. However, the loss and damage were not proximately caused by these conditions, although they may have had some contributing effect.

### Issues of Law

A. Was the placing and leaving of the wood cart within 42 inches from the track a breach of the contract by defendant?

That is a trick question, but I answer it as follows: Yes, under all the surrounding circumstances, since the loss to plaintiff was a direct and proximate result.

B. Is plaintiff entitled to be indemnified by defendant under the industrial track agreement in the sum of \$46,568.99, or any part thereof?

No, not as such.

C. Is defendant obligated to pay plaintiff \$46,-



568.99, or any part thereof, independent of the agreement?

No, not as such.

D. Can an employer under the Federal Employers Liability Act delegate the duties imposed upon him under the Act?

That question, in the Court's opinion, has no relevance to the situation, but the answer is No, not between the railroad and the employee.

E. Is the negligence imposed upon an employer for violation of the Federal Employers Liability Act, resulting in injuries to an employee, considered to be primary negligence?

I do not understand that question, but the Court rules that in the action between other parties if there was a violation of the Federal Employers Liability Act the injured employee would be entitled to recover in that action, but there is no relevancy between that situation and this case between other parties.

F. Can a railroad operating as a common carrier contract to be held harmless against its own negligence, or is such a contract void as against public policy?

This contract is valid even though the acts of employees of plaintiff may have contributed to and resulted in the injury to Powers.

G. Whose control was the track under, and did the track area include the point and place where the cart was located?

This is another catch question which the Court considers entirely immaterial and therefore disregards.

H. Did the railroad have the right to have any obstructions removed which the railroad deemed hazardous?

Yes.

I. Was there a waiver of any breach, if one existed?

No.

The Court finds, using the verdict as advisory, that Powers suffered injuries in the sum of \$44,000.00. The acts and omissions of the defendant were the direct and proximate cause thereof. The acts and omissions of plaintiff contributed thereto in some measure. Plaintiff paid out a greater sum than the damage found. Therefore, the Court awards \$22,000.00 to plaintiff on the contract.

[Endorsed]: Filed Aug. 19, 1949.

[Title of District Court and Cause.]

## REPORTERS' CERTIFICATE

We, Ira G. Holcomb and John S. Beckwith, Official Reporters of the above-entitled Court, do hereby certify that on the 11th and 12th days of November, 1948, and on the 13th day of June, 1949, we reported in shorthand certain proceedings had in the above-entitled matter, that we thereafter caused our respective shorthand notes to be reduced to typewriting under our direction, and that the foregoing transcript, consisting of Pages numbered 1 to 67, both inclusive, constitutes a full, true and accurate transcript of said proceedings, the respective portions of which transcribed by each of us are as follows: Pages 1 to 60, Ira G. Holcomb; Pages 61 to 67, John S. Beckwith, so reported by us in shorthand on said dates, as aforesaid, and of the whole thereof.

Dated this 13th day of August, A.D. 1949.

/s/ IRA G. HOLCOMB,

/s/ JOHN S. BECKWITH.

## CERTIFICATE OF CLERK

United States of America,  
District of Oregon—ss.

I, Lowell Mundorff, Clerk of the United States District Court for the District of Oregon, do hereby certify that the foregoing documents consisting of

complaint, answer, pre-trial order, findings of fact and conclusions of law, judgment order, notice of appeal, bond on appeal, notice of cross-appeal, bond on cross-appeal, order to send original exhibits, appellant's designation of record, transcript of docket entries, and clerk's certificate, constitute the record on appeal from a judgment of said court in a cause therein numbered Civil 3989, in which The Booth-Kelly Lumber Company is defendant and appellant, and the Southern Pacific Company is plaintiff and appellee; that the said record has been prepared by me in accordance with the designation of contents of record on appeal filed by the appellant, and in accordance with the rules of this court.

I further certify that there is enclosed herewith duplicate transcript of proceedings dated November 11 and 12, 1948, and June 13, 1949, together with exhibits 1, 2a, 2b, 2c, 2d, 2e, 2f, 2g, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 14, 15, 18, inclusive.

I further certify that the cost of preparing the within transcript is \$1.60, and the cost of filing the notice of appeal is \$5.00, making a total of \$6.60, and that the same has been paid by the appellant.

In Testimony Whereof I have hereunto set my hand and affixed the seal of said court in Portland, in said District, this 26th day of August, 1949.

[Seal]

LOWELL MUNDORFF,

Clerk.

By /s/ F. L. BUCK,

Chief Deputy.



[Endorsed]: No. 12340. United States Court of Appeals for the Ninth Circuit. Booth-Kelley Lumber Company, a Corporation, Appellant, vs. Southern Pacific Company, a Corporation, Appellee, and Southern Pacific Company, a Corporation, Appellant, vs. Booth-Kelley Lumber Company, a Corporation, Appellee. Transcript of Record. Appeals from the United States District Court for the District of Oregon.

Filed August 29, 1949.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for the  
Ninth Circuit.

In the United States Court of Appeals  
for the Ninth Circuit

No. 12340

BOOTH-KELLY LUMBER COMPANY,  
Plaintiff,

vs.

SOUTHERN PACIFIC COMPANY,  
Defendant.

and

SOUTHERN PACIFIC COMPANY,  
Plaintiff,

vs.

BOOTH-KELLY LUMBER COMPANY,  
Defendant.

DESIGNATION OF RECORD TO BE  
PRINTED ON APPEAL HEREIN.

It Is Stipulated by and between the attorneys for the respective parties hereto that the following be printed as a record of appeal herein, omitting therefrom headings, titles and such formal matters:

1. Pleadings.
2. Pre-trial Order.
3. Reporter's Transcript of entire trial proceedings.
4. Findings of Fact and Conclusions of Law and Judgment Order entered thereon.

5. Opinion of the Court.

6. Notice of Appeal and cross-Appeal.

/s/ JAMES ARTHUR POWERS,  
Of Attorneys for Booth-Kelly  
Lumber Company.

/s/ ALFRED H. CORBETT,  
Of Attorneys for Southern  
Pacific Company.

[Endorsed]: Filed Sept. 21, 1949.

---

In the United States Court of Appeals  
for the Ninth Circuit

Case No. 12340

BOOTH-KELLY LUMBER COMPANY,  
a Corporation,

Appellant-Defendant.

vs.

SOUTHERN PACIFIC CORPORATION,  
a Corporation,

Cross-Appellant-Plaintiff.

### STIPULATION

It Is Stipulated By And Between the attorneys  
for the respective parties hereto that the original  
exhibits received in evidence upon the trial in the  
lower court, together with original exhibits marked  
for identification therein but not received in evi-

dence may be considered by the Court in the within appeal in their original form.

/s/ JAMES ARTHUR POWERS,  
Of Attorneys for  
Appellant-Defendant.

/s/ ALFRED H. CORBETT,  
Of Attorneys for  
Cross-Appellant-Plaintiff.

So Ordered:

/s/ WILLIAM HEALY,  
/s/ HOMER T. BONE,  
/s/ WALTER L. POPE,  
United States Circuit Judges.

[Endorsed]: Filed Oct. 20, 1949.

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[Title of Court of Appeals and Cause.]

STATEMENT OF POINTS UPON WHICH  
APPELLANT WILL RELY ON APPEAL.

Appellant Booth-Kelly Lumber Company will rely upon the following points on appeal:

I.

1. That there was no breach of contract. Appellee's loss did not result through breach by Appellant of the contract. Any breach of the contract was fully known to Appellee and was waived by it.

2. (a) Appellee is estopped by its conduct from asserting that alleged breach of contract caused its



loss as a custom of operation had been developed between the parties covering the removal of any obstruction to track clearance upon request of Appellee.

(b) That the claimed breach of clearance was discovered by Appellee long prior to damage and therefore such damage was not caused by the claimed breach.

3. Appellee's loss resulted solely through an act or omission of Appellee and through no act or omission of Appellant.

4. That the judgment in the California Action is binding upon the parties as to the cause of Appellee's loss and the matter cannot be relitigated in the Federal Court.

5. No recovery can be allowed Appellee under the contract as it is an attempt to contract against its own negligence, the contract is void as against public policy under the laws of the State of Oregon as otherwise it would permit Appellee to recover for a loss it sustained through its own negligence.

6. (a) Negligence established in the California action, in action of employee against Appellee, constitutes the immediate proximate cause of the accident and injury, and Appellant's negligence, if any, is a mere remote cause; that matter is now res adjudicata.

(b) Appellee's liability to its injured workman did not arise out of the track agreement but rather

out of the master-servant relationship between Appellee and its injured employee under the Federal Employer's Liability Act.

7. There is no consideration for the contract and a total lacking of mutuality for the indemnity provision contained therein.

8. The contract has no application because the indemnity provision thereof, namely Paragraph VII, is applicable only when railroad (Appellee) is serving industry and at the time of the accident railroad (Appellee) was not serving industry.

/s/ JAMES ARTHUR POWERS,  
Of Attorneys for Appellant.

Receipt of copy acknowledged.

[Endorsed]: Filed Oct. 31, 1949.

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[Title of Court of Appeals and Cause.]

STATEMENT OF POINTS UPON WHICH  
CROSS-APPELLANT WILL RELY ON  
APPEAL.

The points upon which cross-appellant intends to rely on this appeal are as follows:

1. The court erred in failing to enter judgment against appellant, for breach of the indemnity provisions of the spur track agreement, in the sum of \$46,568.99, the amount of loss suffered by cross-appellant by reason of an act or omission of appel-

lant its agents or employees to an employee of cross-appellant while on the industrial spur; or, in the alternative.

The court erred in failing to enter judgment against appellant for breach of the indemnity provisions of the spur track agreement, in the sum of \$23,284.49, one-half the amount of loss suffered by cross-appellant by reason of an act or omission of appellant, its agents or employees to an employee of cross-appellant while on the industrial spur.

2. The court erred in failing to award damages to cross-appellant in the sum of \$46,568.99 for breach of the impaired clearance provisions of the industrial spur track agreement.

3. The court erred in failing to award recovery to cross-appellant in the sum of \$46,568.99 independent of contract, because appellant's negligence in placing and leaving the wood cart within 42" from the spur track was the active, direct, proximate and primary cause of the injury to cross-appellant's employee Powers, and of cross-appellant's resulting liability.

/s/ ALFRED H. CORBETT,

Of Attorneys for Cross-Appellant.

Service of copy acknowledged.

[Endorsed]: Filed Nov. 5, 1949.





No. 12340

In The  
**United States Court of Appeals**  
**For the Ninth Circuit**

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Appellee.*

and

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Appellant,*

vs.

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Appellee.*

Appeal from the District Court of the United States for  
the District of Oregon

HONORABLE JAMES ALGER FEE, *Judge*

**Brief of Appellant Booth-Kelly Lumber Company**

KOERNER, YOUNG, SWETT & MCCOLLOCH,  
JAMES C. DEZENDORF,  
ALFRED H. CORBETT,  
800 Pacific Building, Portland, Oregon,  
*Attorneys for Appellee.*

VEAZIE, POWERS & VEAZIE, and  
JAMES ARTHUR POWERS,  
611 Corbett Building, Portland, Oregon,  
*Attorneys for Appellant.*

FILED

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No. 12340

**In The  
United States Court  
of Appeals  
For the Ninth Circuit**

---

BOOTH-KELLY LUMBER COMPANY, a Corporation, *Appellant*,  
vs.

SOUTHERN PACIFIC COMPANY, a Corporation, *Appellee*,  
and

SOUTHERN PACIFIC COMPANY, a Corporation, *Appellant*  
vs.

BOOTH-KELLY LUMBER COMPANY, a Corporation, *Appellee*.

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Appeal from the District Court of the United States for the  
District of Oregon

HONORABLE JAMES ALGER FEE, *Judge*

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**Brief of Appellant Booth-Kelly Lumber Company**

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**JURISDICTIONAL STATEMENT**

This is an action at law between citizens of different states, (Pre-trial Order, T. 33) in which the appellee corporation claims damages of \$46,568.99 against the appellant corporation. (Pre-trial Order, T. 37) Judgment in the sum of \$22,000.000 has been entered, based

upon findings of fact and conclusions of law made and entered by the court. (Judgment Order, T. 56) It is contended that the United States District Court for the District of Oregon has jurisdiction of this action on the basis of the above facts, under 28 U.S.C.A., section 1332 (a) (1); and that the United States Court of Appeals for the Ninth Circuit has jurisdiction of this appeal, under 28 U.S.C.A. sec. 1291. (T. refers to transcript of record.)

### STATEMENT OF THE CASE

(Appellant is referred to herein as "Booth-Kelly" or "Industry"; Appellee is referred to herein as "Southern Pacific" or "railroad.")

Powers, a brakeman, was injured while employed by Southern Pacific in switching operations on a spur track near Springfield, Oregon. The accident occurred February 8, 1945. At the time of the accident Southern Pacific was carrying on operation for its own benefit in serving a third party; Southern Pacific was doing nothing on behalf of Booth-Kelly or for the benefit of Booth-Kelly at the time of the accident. The Southern Pacific was then acting as a common carrier. The injured brakeman brought an action against his employer, Southern Pacific in the state court in California. Southern Pacific was the sole defendant and the action was based

upon a violation of the Federal Employers' Liability Act. The jury therein found the Southern Pacific liable as employer for failing to provide its employee with a safe place to work, specifically, a failure to warn him that there was a wood cart near the side track. (Admitted Facts, T. 35) The judgment assessed against the Southern Pacific was compromised by paying Powers the sum of \$44,699.45. The recovery in the California Court was based solely on negligence of Southern Pacific. The evidence shows that Southern Pacific continued to operate its trains over said spur track for a period of several days with full knowledge that the cart was there, and in the same position it was in when the accident occurred.

Southern Pacific then filed action against Booth-Kelly in the Oregon Federal District Court for said sum plus \$1,869.53, costs and attorneys' fees. The claim is made in said action that Southern Pacific is entitled to recover from Booth-Kelly under an indemnity provision contained in a spur track agreement. The spur track was a long one and the first 2,257 feet thereof was owned by the Southern Pacific and was used jointly with Booth-Kelly. The accident occurred within about 200 feet from where the spur track joins the main line as a locomotive and caboose were backing up after having delivered five cars of logs to the Springfield Plywood Company. (T. 103, 90) The caboose was a converted box car with no regular steps or railings at the front or back but

merely had a side door with grab-irons which made it necessary for the brakeman to back out and thus expose his body beyond the side door. (T. 95-96) (Reporter's Transcript, P. 145-7, 167, 172.)

The accident occurred when Powers was backing out of the caboose and he was caught between it and a wood cart placed within 42 inches of the track. (Reporter's Transcript, Powers v. Southern Pacific Company, P. 165.) It is contended by the Southern Pacific that the cart was an obstruction forbidden by the track agreement and that therefore Paragraph 7 of the agreement comes into effect requiring Booth-Kelly to indemnify the railroad for Power's injuries. (T. 11) In their view the failure of the railroad, specifically of Power's conductor and the other three members of the crew, to notify Powers of a fact which they admittedly all knew, namely the proximity of the cart to the track, does not bar the railroad's recovery over. (Reporter's Transcript, P. 130, 283.) Yet this failure to warn was the sole basis for the judgment in the California action since any question of the railroad's responsibility for the location of the cart was excluded. (Admitted Facts, T. 35.)

To summarize, both parties rely on the judgment in the California action and deem themselves bound thereby. (Admitted Facts, T. 36.) One of the basic questions for decision is the effect of that judgment in this action,



in view of the admitted fact Booth-Kelly was tendered the defense of the California action but did not assume it. (T. 35) We contend that the judgment there shows the Southern Pacific's failure to warn to be the sole basis of Power's recovery and further that the railroad's failure to warn was the proximate cause of Power's injuries.

The second basic question is the validity and applicability of the indemnity provision of the contract. The agreement in force at the time of the accident was entered into on or about June 30, 1941, but it is the Southern Pacific's redraft of two agreements made in 1909 which are terminated by it. (T. 19) The track had been constructed on the "old" industrial basis by which the railroad furnished the metal and the future maintenance. We contend that same basis was laid down in two Oregon statutes which are now codified as 8 O.C.L.A. sec. 113-108, 109, 110.

Those statutes plus 8 O.C.L.A. sec. 113-104 require the railroad as a common carrier in Oregon to furnish side track service. (Texts set out in the brief.) In the 1941 agreement the railroad as a part of the redrafting inserted a new provision, the indemnity clause (Paragraph 7). (T. 11) We contend that both the legal requirement of service and the unilateral modification of the contract amount to a lack of consideration for the indemnity agreement.

The meaning and validity of the clause so far as it pertains to third person injuries is basis of most of the controversy here. However, Paragraph 7 must be construed in conjunction with Paragraph 4 which gives the railroad control of the track and the right to use it to serve others than Booth-Kelly. (T. 8) In fact the track was used to serve the Springfield Plywood Company and the Huntington Shingle Mill and for general switching purposes. (T. 89, 105) Furthermore, since the first sentence in Paragraph 7 specifically restricts its application to when the railroad is serving Booth-Kelly, the second sentence in the paragraph is also so restricted. Finally we contend that the indemnity clause as it was construed and applied below violates the Oregon rule that it is against public policy for a person to be indemnified against his own negligence.

The third basic question is the construction of the contract apart from the indemnity clause. There was no breach of the contract to bring the indemnity clause into play since the words of Paragraph 5 as to clearance do not cover the situation here presented, a moveable cart. (T. 8) Secondly, as a matter of law the location of the cart, if it was a breach, did not cause the accident since the Appellee knew of the breach long prior to the accident. (T. 54) Finally the breach, if any, was waived by the Appellee and in addition Appellee is estopped by

a failure to conform to the customary method of removing obstructions.

The case came on for trial in the Oregon District Court before Judge James Alger Fee sitting without a jury on November 11, 1948. On the same day a Pre-trial Order, agreed upon at a conference between counsel and the Court, was approved and entered. It was ordered that the Pre-trial Order supersede the pleadings. Defendant moved for an involuntary non-suit based upon the following propositions resulting from analysis of the Transcript in *Powers v. Southern Pacific Company* (Exhibits 2c, 2d, 2c); in summary they are: that the primary negligence was found to be on the Southern Pacific Company; that all the negligent acts concerned the Southern Pacific Company; that there was a duty on the part of the railroad; that the action was brought under the Federal Employers' Liability Act; and the jury found under the charge that the negligence of the Southern Pacific Company proximately caused the injury complained of and judgment was entered on the basis that Southern Pacific's negligence was the proximate cause of the injury, or the Southern Pacific's negligence combined with the negligence of the injured man, proximately caused the accident. (T. 66) Motion for involuntary non-suit was overruled, and exception taken. (T. 77).

After the plaintiff rested, the defendant moved for

a directed verdict. (T. 112) (Court denoted it a motion for judgment as a matter of law. T. 113.) Motion was based on the following grounds (summarized): that under the law plaintiff is not entitled to recover on any of its counts; that it appears from the evidence that they have submitted and under the stipulation the primary cause or loss was the railroad company's own negligence, and that a common carrier cannot recover under such a contract if it is a loss suffered through its own negligence or, for that matter, the negligence of the company combined with that of anyone else; that when the accident occurred logs were being moved for the Springfield Plywood Company and all agreements, starting with the earliest, consistently reserve to the railroad the right to use the railroad in its own business and that there is nothing in the contract which makes clear that if the railroad was doing something for its own benefit, operating as a common carrier, hauling other people's freight, that this defendant would not be required to indemnify the railroad; that one tortfeasor can't recover from the other, under the laws of Oregon; and further on all the grounds previously mentioned in connection with the motion for a non-suit are here incorporated. (T. 112-113) The motion for a directed verdict was denied. (T. 113)

On June 22, 1949 the court filed its Findings of Fact and Conclusions of Law and a judgment order for the



plaintiff was entered in sum of \$22,000.00 plus costs and disbursements taxed at \$27.64. On July 22, 1949 the defendant filed notice of appeal and the plaintiff filed notice of cross-appeal.

All questions raised are by objections to certain of the court's Finding of Fact and Conclusions of Law which are set out particularly in the brief under each specification of error.

### **SPECIFICATION OF ERROR NO. I**

The judgment in the California Action is binding upon the parties as to the cause of Appellee's loss and the matter cannot be relitigated in the Federal Court. (Appellant's Appeal Point 4, T. 129)

Specifically the court erred as it made the following Finding of Fact without any evidence to support it:

"The loss and damage to Powers were not proximately caused by the conditions mentioned in the previous findings." (Previous to Finding of Fact 18) (Findings of Fact # 18, T. 54)

The court further erred as a matter of law in making and entering the following Conclusion of Law:

"The determinations in the Mack D. Powers' action against plaintiff are not res adjudicata in this proceeding." (Conclusion of Law # 2, T.55)



## SUMMARY OF ARGUMENT OF THE ABOVE SPECIFICATION OF ERROR

**POINT ONE:** Principle of res judicata as to the first action now binds indemnitee railroad.

**POINT TWO:** Where a corporation is responsible over to another corporation by an express contract of indemnity and is notified of the pendency of a suit against the indemnitee and the defense of that suit is tendered the indemnitor, the indemnitor will be bound by the issues decided in the first action when the indemnitee in a second action sues the indemnitor on the contract. The rule that privity is necessary for estoppel by judgment has an exception where a person having a derived liability like the indemnitor corporation is concerned; therefore all issues necessarily decided in the first action are res judicata as against the notified indemnitor corporation.

### ARGUMENT: POINT ONE

The indemnitee railroad is bound by the findings of the first action as to any negligence of which it was there found guilty. As will be shown subsequently, the railroad was held in *Powers v. Southern Pacific Company* for its sole negligence. We now cite authority to show that such findings are now res judicata as to the

railroad. First the railroad *agreed* below that “both parties to this action are bound by the proceedings and judgment in the action, Mack D. Powers v. Southern Pacific Company as to all matters there determined.” (Pretrial Order, Admitted Facts, Par. IX, T-36.)

Second as a matter of law the indemnitee is bound by the determinations there adverse to its claim for indemnity. By way of introduction the Restatement of the Law of Judgments may be helpful. Section 107 is concerned with the “Rights of Indemnatee and Indemnitor Inter Se after Judgment against One of Them.” (P. 511) Comment h (Findings adverse to indemnitee’s claim for indemnity) on that section is particularly in point here (P. 517):

“In actions between the indemnitor and indemnitee, the indemnitee is subject to the burdens, as well as entitled the benefits, of the rules of res judicata with reference to the matters determined in an action brought by the obligee or by the injured person. If the judgment is based on a finding of fact which if correct would discharge the indemnitor, the latter is discharged from liability to the indemnitee by such finding, unless by agreement the entire defense is controlled by the indemnitor.”

The comment continues on page 518 with an illustration applicable to the facts here:

“So where a person has been hurt by a telephone wire which was electrified by touching a power wire

and the injured person sued the telephone company and judgment was given against the telephone company on the ground that it knew of the danger, the telephone company, which had unsuccessfully invited the power company to defend the action, is bound by the finding in its subsequent action for indemnity against the power company."

Nor is authority lacking that the indemnitee is bound by what was decided in the first action. In *Edinger & Co. v. S. W. Surety Insurance Co.*, 182 Ky. 340, 345, 206 S.W. 465, the court is explicit on the point:

"If the judgment in one state of facts will be conclusively binding on the insurance company (indemnitor) on the theory that it established its liability, we perceive no reason why the judgment on another state of facts that excused it from liability would not be conclusively binding on Edinger & Company (indemnitee)." (Insertions added.)

In that case it was held that the insurance company was not liable to indemnify Edinger & Company because the first action established a fact as to the subject of insurance which put the damage within an exemption clause in the policy.

In *Central of Georgia Ry. Co. v. Macon Ry. & Light Co.*, 9 Ga. App. 628, 71 S. E. 1076, a Central railroad employee was electrocuted when a worn electric wire crossed a coal chute cable which he was pulling in order

to load a locomotive tender. The court's syllabus (Par. 5) summarizes as follows:

"Where a right of action over against a third person is asserted by the defendant in a prior tort action who has been compelled by the judgment thereon to pay damages, the plaintiff in the second action is estopped from showing that the causes alleged in the prior action were not the true causes of the damages." (P. 629)

To like effect is the court's assertion in *Hudson Valley Ry. Co. v. Mechanicville E. L. & G. Co.*, 101 Misc. Rep. 152, 166 N.Y.S. 816, 817, *reversed on other grounds*, 180 App. Div. 86, 167 N.Y.S. 428, that since the action was based on the judgment in the prior case

"plaintiff may not deny or contradict the facts, upon which it was recovered, with other facts, but must accept the findings there made upon the questions there litigated and determined (citations)."

Upon the basis of the above authorities it would seem that the plaintiff below must accept what the California jury found to be the cause of the damage and is now estopped to show that the cause of Powers' injuries is any other than that which we will show the jury found, namely, a failure to warn.

**ARGUMENT: POINT TWO**

The leading case for the proposition that where a party is responsible over to another, and is duly notified of the suit, he will be bound by a judgment fairly obtained against the other, is *Littleton v. Richardson*, 34 N.H. 179, 187. The following excerpt from that case is often quoted as representative of the law:

“But when a person is responsible over to another, either by operation of law or by express contract — (citation) — and he is duly notified of the pendency of the suit and requested to take upon him the defense of it, he is no longer regarded as a stranger, because he has the right to appear and defend the action, and has the same means and advantages of controverting the claim as if he was the real and nominal party upon the record. In every such case, if due notice is given such person, the judgment, if obtained without fraud or collusion — (citation)—will be conclusive against him, whether he appeared or not; (citation). Of every fact established by it; (citations) . . .”

The United States Supreme Court has adopted that rule. In *Washington Gas Light Co. v. Dist. of Columbia*, 161 U.S. 316, 329, 16 S. Ct. 564, 40 L. Ed 712, the court said:

“As a deduction from the recognized right to recover over, it is settled that where one having such right is sued, the judgment rendered against him is conclusive upon the person liable over, provided notice is given to the latter, and full opportunity be afforded him to defend the action. There



is here no question of the sufficiency of the notice, or of the ample adequacy of the opportunity given the Gas Company to defend the suit had it elected to do so.

“In both *Chicago v. Robbins* and *Robbins v. Chicago, ub. sup.*, (2 Black 418, (U.S. 1862), 4 Wall. 657 (U.S. 1866).) this court, after announcing this rule as to the liability over in the language already quoted, also held that where, in the first suit, proper notice was given to the party liable over, the first judgment would be conclusive against the latter in the action to recover.” (citations added)

The Oregon court in *Astoria v. Astoria & Columbia R. Co.*, 67 Or. 538, 136 Pac. 645, adopted the rule that the first judgment is conclusive on the person liable over who is defendant in the second suit as to all subjects in controversy in the first action. In that case a pedestrian had recovered from the city for an injury sustained due to the way in which a railroad track was placed in a public street, the railroad company having been granted a right of way on the street. Here as there the party allegedly ultimately liable was notified and requested to assume the defense of the action and in both cases refused. (Pretrial Order, Admitted Facts, Paragraph V)

The court said at P. 549:

“4. The next question to be considered concerns the legal effect to be given to the judgment obtained by Annie Anderson against the City of Astoria in the United States Circuit Court for Oregon. The lower

court advised the jury that the judgment was conclusive evidence of the following facts . . . . . An examination of the pleadings in the original case reveals that the issues which the court told the jury were conclusive on defendant were all subjects of controversy therein. *Consequently the judgment in that action is conclusive of the facts thereby established and could not again be the subject of litigation between plaintiff and defendant if the latter was notified of the former action. The scope of the estoppel created by the judgment in the primary case embraces all of the issues determined by it.*" (emphasis supplied)

Nor does the Astoria case stand alone in Oregon. In *Riggs v. New Jersey Plate Glass Co.*, 126 Or. 404, 416, 270 Pac. 479. The Court said:

"13. Where the indemnitor is notified of the pendency of an action against the indemnitee in reference to the subject matter of the indemnity and is given an opportunity to, and does defend such action, the judgment in such action if obtained without fraud and collusion, *is conclusive upon the indemnitor as to all questions determined therein which are material to a recovery against him in an action for indemnity brought by the indemnitee*: 31 C.J. 460; Section 60. See *Fenton v. Fidelity & Cas. Co.*, 36 Or. 283 (56 Pac. 1096, 48 L.R.A. 770); *Astoria v. Astoria & Col. Riv. R. R. Co.*, 67 Or. 538 (136 Pac. 645, 49 L.R.A. (N.S.) 404)." (emphasis supplied)

In 40 L. R. A. (N.S.) 1172 a note on the "Conclusiveness of judgment against a constructive tortfeasor in a subsequent action for contribution or indemnity" says of "notice or its equivalent" (P. 1174):

“Where the present defendant had notice of the former suit or its equivalent, the judgment therein is conclusive upon him, so far as it relates to matters necessarily included in the adjudication.” (citing many cases)

That is the law in Oregon: *Riggs v. New Jersey Plate Glass Co.*, *supra*; *Astoria v. Astoria & Columbia River R. Co.*, *supra*.

133 A.L.R. 181 annotates “judgment in action growing out of accident as *res judicata*, as to negligence or contributory negligence in a later action growing out of same accident by or against one not a party to earlier action”. The subtopic “VI.a. Defendant in earlier action as plaintiff in action against new party, 190” is particularly in point here. The point of the annotation for our purposes is summarized at page 196:

“A judgment for the plaintiff in an action arising out of an accident has been held to be *res judicata*, or *conclusive*, as to the issue of negligence, against one not a party to such action but made a defendant in a subsequent action as derivatively responsible.” (emphasis supplied)

See also 123 A.L.R. 704, Judgment in action by third person against insured as *res judicata* in favor of indemnity or liability insurer which was not a nominal party.

The language of the cases is usually that the first judgment is “conclusive” on the indemnitor when the

indemnatee sues. By this is meant that the first judgment is *res judicata*. For example throughout the above annotation, 133 A.L.R. 181, as we have emphasized in the last quotation "*res judicata* or conclusive" have consistently been used as alternative equivalent formulas. (Pages 184, 190, 192) An eminent treatise writer writes:

"When it is said that judgment in this class of cases is conclusive on the person notified, the statement must of course be considered in connection with the general principles which determine the effect of judgment as *res judicata*." 1 Freeman, *Judgments*, Section 450 (5th Ed. 1925) 991.

Lest there be any confusion it should be noted that the court in its Conclusion of Law said that the determinations in the earlier action were not "*res adjudicata*". According to Black's Law Dictionary (3rd Ed. 1933) 1538 "*res adjudicata*" is a

"common but indefensible misspelling of *res judicata*. The latter term designates a point or question or subject-matter which was in controversy or dispute and has been authoritatively and finally settled by the decision of a court."

The general rule is that there must be mutuality of estoppel if the judgment in the first action is to be *res judicata* in the second action: "the strict rule however that a judgment operates as *res judicata* only in regard to parties and privies, has been expanded in many cases



to include others, as those occupying a position of derivative responsibility only . . . .” 112 A. L. R. 404.

Although the general language of the cases is that the first judgment is “conclusive” on the indemnitor in the second action, some cases specifically call the earlier decision *res judicata*. *Hartford Acc. & Indemnity Co. v. First Nat. Bank & T. Co.* 281 N.Y. 162, 22 N.E. 2d 324; *City of Seattle v. Peterson & Co.*, 99 Wash. 533, 170 Pac. 140. The following cases support the proposition that the first judgment against the indemnitee is conclusive or *res judicata* in the second action when the indemnitee sues his indemnitor; and the fact situations involved are analogous to that in the case at bar (except in *State Bank v. American Surety Co.*, 206 Minn. 137, 288 N.W. 7):

*Boston & M.R.R. v. Brackett*, 71 N.H. 494, 53 Atl. 304;

*Boston & M.R.R. v. T. Stuart & Son Co.*, 236 Mass. 98, 127 N.E. 532;

*Missouri, K. & T. Ry. Co. v. Ellis*, 78 Okla. 150, 189 Pac. 363;

*West Jersey & S.S.R. Co. v. Atlantic City Electric Co.*, 107 N.J.E. 457, 153 Atl. 254;

*Hudson Valley Ry. Co. v. Mechanicville Electric Light & Gas Co.*, *supra*;

*Sanitary Dist. v. U. S. Fidelity & Guar. Co.*, 392 Ill. 602, 65 N.E. 2d 364;

*Keller v. City of Fargo*, 49 N.D. 562, 192 N.W. 313.



In summary then as the Oregon court points out in *Astoria v. Astoria & Columbia R. Co.*, *supra*, the judgment in the primary action creates an estoppel as to the indemnitor on all the issues determined by it. The basis of res judicata is estoppel. 15 R.C.L. 960. Since the notified indemnitor is estopped by his failure to defend against the first judgment, the material issues decided in the first action are res judicata in the second action. This rule of conclusiveness is no different where a foreign judgment is involved. *U.S. Fidelity Co. v. Martin*, 77 Or. 369, 149 Pac. 1023.

### **SPECIFICATION OF ERROR NO. II**

Appellee's loss resulted solely through an act or omission of Appellee and through no act or omission of Appellant. (Appellant's Appeal Point 3, T-129)

(a) Negligence established in the California action, in action of employee against Appellee, constitutes the immediate proximate cause of the accident and injury, and Appellant's negligence, if any, is a mere remote cause; that matter is now res adjudicata.

(b) Appellee's liability to its injured workman did not arise out of the track agreement but rather out of the master-servant relationship between Appellee and its injured employee under the Federal Employer's Liability Act. (Appellant's Appeal Point 6, T-129-130)

Appeal points 3 and 6 raise questions which are substantially alike, and to the end of brevity and con-

venience we consolidate our argument thereon, treating them as a single specification of error.

Specifically the court below erred as it made the following Findings of Fact without any evidence to support them:

“Defendant was negligent in placing and leaving the wood cart within 42 inches from the spur track.”

“Defendant’s negligence in this regard was the active, direct, proximate and primary cause of the injury to plaintiff’s employee Powers.” (Findings of Fact #9 & 10, T-53)

### **SUMMARY OF ARGUMENT OF THE ABOVE SPECIFICATION OF ERROR**

**POINT ONE:** Applying the principles of *res judicata* to **POWERS V. SOUTHERN PACIFIC COMPANY**, it is now *res judicata* that the Southern Pacific Company was there held for its own **SOLE** negligence as employer under the Federal Employers’ Liability Act in failing to warn its employee, Powers, of a dangerous working condition. Under the spur track indemnity agreement no recovery can be had for damage suffered where such damage results from the **SOLE** negligence of the indemnitee railroad corporation.

**POINT TWO:** Applying the principles of *res judicata* to **POWERS V. SOUTHERN PACIFIC COMPANY**, it is now *res judicata* that the railroad’s

negligence was the immediate proximate cause of the accident and injury.

### ARGUMENT: POINT ONE

It is now necessary to analyze exactly what was decided in the suit of *Powers v. Southern Pacific Company*, No. 344915, in the San Francisco Superior Court of the State of California. In the Pre-Trial Order, paragraph IV of the Admitted Facts is as follows:

#### “IV.

“Said employee brought action against Southern Pacific Company for damages for his injuries under the provisions of the Federal Employer’s Liability Act. The complaint alleged breach of Southern Pacific Company’s statutory duty of using ordinary care to provide said Mack D. Powers with a reasonably safe place in which to work in that, first, it caused and permitted the wood cart to remain on the track, and second, it failed to warn him of the presence of the wood cart and the resultant insufficient clearance.

“At trial the allegation that Southern Pacific Company placed the wood cart on the track was removed from the jury’s consideration because of lack of evidence. A verdict was returned for said Mack D. Powers.

“The records of said proceeding, consisting of pleadings, transcript of proceedings at trial, verdict and judgment are marked pre-trial Exhibits 2a to 2g, both inclusive.” (T. 34-35)

The court in its Findings of Fact adopted all of the above paragraph IV as its finding "4", except for the last paragraph thereof pertaining to the records of the prior proceeding. (T. 52)

The suit in California was thus based solely on a statute providing for the liability of the *employer* only. The court charged the jury:

"This case is being tried under the rules of law set forth in the Federal Employers' Liability Act, Title 45, Section 51, U.S.C.A. This law is the exclusive remedy applicable to the facts in the case before you. \* \* \* the Federal Employers' Liability Act makes recovery absolutely dependent upon the proof of negligence of the employer, \* \* \*" (Reporter's Transcript, *Powers v. Southern Pacific Company*, pp. 344-5). (45 U.S.C.A. sec. 51, pertinent part set out in appendix)

The complaint there as drawn sets forth the failure to provide a safe place to work in its two aspects as two separate and distinct causes of action. Paragraph V of the first part of the complaint sets forth the first cause of action alleging in substance that the defendant railroad negligently left a wood cart so close to the track that there was insufficient clearance for the brakeman's body and that as a direct and proximate result the plaintiff was injured. (Complaint, *Powers v. Southern Pacific Company*, p. 2) Paragraph II of the second part of the complaint alleges in substance that the defendant railroad neglected to warn the plaintiff of the presence



of the wood cart and the resultant insufficient clearance and that as a direct and proximate result thereof plaintiff was injured. (Complaint, *Powers v. Southern Pacific Company*, p. 4)

In the charge the court instructed the jury that:

“Under the terms of the Federal Employers’ Liability Act, if you find that the defendant was guilty of any negligence whatsoever as alleged in either of the causes of action set forth in plaintiff’s complaint, and further find that such negligence proximately contributed to plaintiff’s being injured, then your verdict must be in favor of plaintiff and against defendant.” (Reporter’s Transcript, *Powers v. Southern Pacific Company*, p. 364)

The jury found in favor of the plaintiff establishing that the defendant railroad was guilty of some negligence which proximately contributed to the plaintiff’s being injured.

The critical question is for just what negligence did the jury hold the defendant railroad. The court in its charge excluded any question of the railroad’s liability on the first cause of action for negligently causing and permitting wood cart to remain too close to the track. After reciting the undisputed facts that the railroad did not place the cart in position and the cart was not on the railroad’s premises, the court said:

“\* \* \* therefore, you are instructed, as a matter of law in this case, that neither defendant Southern Pacific Company, nor any of its agents or servants



or employees, caused the wood cart to be in the position in which it was at the time it struck plaintiff." (Reporter's Transcript, *Powers v. Southern Pacific Company*, p. 355)

Not only was the jury instructed that it could not hold the railroad for creating the condition by placing the cart, but it was further instructed that the railroad had no right to remove the cart once it was placed. For the court, after summarizing various admitted facts as to the ownership and location of the cart and as to who placed the cart, charged that:

"It is further an admitted fact that the cart was not placed in position by Southern Pacific Company. In these circumstances, I instruct you, as a matter of law, that Southern Pacific Company had no right to remove that cart, and in this sense, Southern Pacific Company cannot be charged with responsibility for permitting the wood cart to be or remain in the position in which it was placed." (Reporter's Transcript, *Powers v. Southern Pacific Company*, p. 352)

It would then seem clear that the negligence for which the railroad was held consisted in its failure to warn since it neither *caused* nor *permitted* (in that it had no right to remove) the cart to remain too close to the track as Paragraph V of the complaint setting forth the first distinct cause of action alleges. (Complaint, p. 2)

To summarize then the judgment in the first case was *res judicata* of the fact that the railroad was held liable as an employer for negligently failing to warn its

employee of a dangerous condition. Under the Federal Employers' Liability Act that duty rested on the employer alone. 45 U.S.C.A., sec. 51, sec. 55 (pertinent parts set out in appendix) The second paragraph in clause 7 of the spur track agreement was the main reliance of the plaintiff railroad below. It consists of two parts:

(1) "Industry also agrees to indemnify and hold harmless Railroad for loss, damage, injury or death from any act or omission of Industry, its employes or agents, to the person or property of the parties hereto and their employes, \* \* \* while on or about said Track;"

(2) "and if any claim or liability, other than from fire, shall arise from the joint or concurring negligence of both parties hereto, it shall be borne by them equally."

(Numbers inserted and format of paragraph altered)  
(T. 11-12)

It seems clear that the failure to warn the brakeman was no duty of this defendant under the facts and pleadings of *Powers v. Southern Pacific Company*. The duty under the Act to provide a safe place to work for the railroad's employee by warning him of any danger was a duty of the railroad. 45 U.S.C.A. sec. 51, sec. 55 (pertinent parts set out in appendix) There was no "act or omission" of this defendant in failing to warn the plaintiff since that was the duty of his employer.

The second clause in the indemnity paragraph pro-

vides for equal sharing of liability for any joint or concurring negligence of both parties. In this case that clause has no application since the recovery was had against the railroad for its *sole* and *non-delegable* duty to warn its employee of any danger in his working condition. The court below recognizes that when in denying defendant's motion for judgment as a matter of law (motion for directed verdict), it says:

"The groundwork (for holding the railroad) apparently was the liability which was imposed upon the Southern Pacific Company by a failure to warn which seems to take it out of the category of things for which it can ask for indemnity \* \* \*" (T. 113-114)

It is submitted that with so much of the court's statement we agree, but when the statement continues as follows we disagree:

"\* \* \* but, on the other hand, the contract is fairly specific with respect to what Booth-Kelly Lumber Company did, indemnifying itself (presumably the railroad) against *all* liability for *any* accident \* \* \*"

(Defendant's Motion for Non-Suit, T. 114) (insertions and emphasis supplied).

We disagree because the court's premise is faulty in that it fails to analyze properly the indemnity paragraph set out above. As an analysis shows, the second clause of the paragraph is the only one which may possibly be in point and that clause clearly does not contemplate

Booth-Kelly bearing "*all* liability for *any* accident."

In summary the second clause as to joint negligence has no bearing here because the California jury held the railroad for a single act of negligence, a failure to warn, and that failure was not a simple failure to warn but an employer's failure to warn. Nor was it just the failure of an employer to warn, but the failure of a special kind of employer under a federal statute of restricted application. Booth-Kelly does not stand as employer to the plaintiff, and so does not concur in negligence to produce damage indemnifiable under the second clause. The railroad was not held for any negligence in leaving the wood cart near the tracks which might be an act or omission of Booth-Kelly within the meaning of the first clause in the indemnity paragraph.

The alleged negligence of this defendant in regard to the wood cart can not be considered settled by the verdict there. "A question in issue cannot be considered settled by the verdict where the jury were instructed that such issue was immaterial." (Headnote) *Bingham v. Honeyman*, 32 Or. 129, 51 Pac. 735, 52 Pac. 755. Here the position of the wood cart was immaterial to the verdict rendered against the railroad since the jury was instructed that the railroad had no control of the cart.

In California, the following rule of *res judicata* was quoted with approval:

"To be a bar to future proceedings it must appear

that the former judgment necessarily involved *the determination of the same fact* to prove or disprove which it is pleaded or introduced in evidence. *It is not enough that the question was one of the issues in the former suit. It must appear to have been precisely determined.*"

*Purcell v. Victor Power etc. Co.*, 29 Cal. App. 504, 510, 156 Pac. 1009.

### FAILURE TO WARN IS AN INDEPENDENT ACT OF NEGLIGENCE

Booth-Kelly's negligence regarding the wood cart was not precisely determined, but on the other hand the negligence of the Southern Pacific in failing to warn its employee was precisely determined as analysis of the record in that case has shown. Two Washington cases clarify the problem involved here. In *City of Seattle v. Peterson & Co.*, 99 Wash. 533, 170 Pac. 140, the city sued a grading contractor on his bond when a customer of the city's electrical system had been shocked as a result of the contractor's blasting which had disturbed the power lines. The customer successfully sued the city, but in the cited case judgment for the defendant contractor was affirmed. The court said of the instructions in the suit against the city at page 141:

"Whether these instructions were right or wrong need not now be inquired into. They became the law of the case and the parties are bound by them. Under these instructions a verdict was rendered



against the city which *established its negligence under the independent act of negligence alleged against it.* (Emphasis supplied.) The judgment entered upon that verdict is conclusive upon that point and is now *res adjudicata.*”

So also here the railroad was adjudged liable under an independent act of negligence alleged against it, a failure to warn its employee. The indemnity agreement of the contractor there is generally similar to the one here, the indemnitor there agreeing to save the indemnitee harmless from all suits for injury or damage sustained by any act or omission of the indemnitor. (P. 140)

In *City of Puyallup v. Vergowe*, 95 Wash. 320, 322, 163 Pac. 779, the court also pointed out the independent negligence of the city which was seeking indemnity:

“It will thus be seen that negligence as to the condition of the street light, which was part of the general lighting system of the city was charged in the complaint; that evidence was submitted thereon; and that the trial judge covered the issue in his instructions to the jury. This issue was determined against the defendant city by a general verdict of the jury and, *a priori, established an independent act of negligence on the part of the city.*” (Emphasis supplied)

The foregoing is applicable here if for the “condition of the street light” we substitute a “failure to warn”. The complaint in the first action had charged the city

with being negligent in having torn up the road (actually done by the contractor) and in not lighting the street. Similarly the railroad here was charged with leaving the wood cart close to the track (actually done by this defendant), and in not warning its employee.

It would seem clear that these two Washington cases established by analogy that the railroad was held in *Powers v. Southern Pacific Company* solely because of an independent act of negligence, the failure to warn. The Washington cases establish that a prior verdict may by implication determine the damage to be caused by an independent act of negligence of the indemnitee.

Here the record in *Powers v. Southern Pacific Company* does establish that the railroad was guilty of a similar independent act of negligence, and as has been shown this independent act of negligence was the sole basis on which Powers had recovery. Under the indemnity clause as drawn here there can be no recovery since it covers only Booth-Kelly's sole act or omission or the joint negligence of the indemnitee and indemnitor. That is not sufficiently explicit in Oregon to cover the indemnitee's own sole negligence.

"If an indemnitee negligently causes injury to a third party and thereby suffers liability and loss by reason of its own sole negligence, it is properly held that he cannot have indemnity in an action on a bond against the indemnitor, unless it is clearly made manifest in the bond that it was intended to cover the indemnitee against his own negligent

acts." *U. S. Fid. & Guar. Co. v. Thomlinson Co.*, 172 Or. 307, 324, 141 P. (2d) 817.

The substance of our contention is that the recovery of Powers against the Southern Pacific rests upon a fact fatal to its recovery here, its own failure to warn its employee. *Boston & M. R. R. v. Brackett*, 71 N.H. 494, 496, 53 Atl. 304. In *American Surety Co. v. Singer Sewing Machine Co.*, 18 F. Supp. 750, 753, the court says:

"\* \* \* if the judgment in the earlier action rested on a fact fatal to recovery in the action over against the indemnitor, the later action against the indemnitor may not be successfully maintained. *Alabama Title & Trust Co. v. Millsap*, 71 F. (2d) 518 (C.C.A. 5); *Gregg v. Page Belting Co.*, 69 N.H. 247, 46 A. 26 *Buffalo Steel Co. v. Aetna Life Ins. Co.*, 156 App. Div. 453, 141 N.Y.S. 1027, affirmed 215 N.Y. 638, 109 N. E. 1067; *Edinger & Co. v. Southwestern Surety Co.*, 182 Ky. 340, 206 S.W. 465."

The failure to warn is a fatal fact here because it prevents the indemnity clause coming into operation since such failure to warn is the negligence of the railroad *solely*.

### ARGUMENT: POINT TWO

*William Cameron & Co. v. Thompson*, ..... Tex. Civ. App. , 175 S.W. 2d 307, involves almost identical facts to this case and should be controlling. There was a spur track indemnity agreement similar to the

one here. A brakeman was injured by a hand truck which rolled out of a freight car as some cars on a spur track were being switched:

“Even if it be negligence to thus leave the hand truck unblocked and the car door unclosed, such negligence could not, as a matter of law, be proximate cause of Benton’s injuries, because the employees of Cameron & Company could not reasonably have contemplated that the switching crew would arrive during their absence and negligently proceed to switch the car without blocking the wheels of the hand truck and closing the door of the car. One is not required to contemplate the negligence of another (citations).” (p. 308)

The court continues on page 309:

“It occurs to us that if the act of the unloading crew in leaving the hand truck in the car with the door open could be regarded as any cause of Benton’s injuries, certainly it was a remote cause, and the proximate cause of such injury was the negligence of the switching crew in failing to properly block the wheels of the hand truck and close the door of the car before beginning switching operations. As was said by Judge Critz in *Phoenix Refining Company v. Tips*, 125 Tex. 69, 81 S.W. 2d 60, 61: ‘prior or remote cause cannot be made the basis of an action for damages if it does nothing more than furnish the condition or give rise to the occasion which makes the injury possible. If such injury is the result of some other cause which reasonable minds would not have anticipated, even though the injury would not have occurred but for such condition.’ (Citing authorities.)”

Here the accident was not such that reasonable minds would have anticipated. The wood cart here had



been in its location at least three or four days and the spur track had been used repeatedly without injury despite its presence:

“One witness said he remembers distinctly going in the day before. Another witness said two or three days before. We know they were in there on the 30th. We know that they were in there pretty regularly, \* \* \*” (Defendant’s Argument, Reporter’s Transcript, *Powers v. Southern Pacific Company*, p. 283-4.)

The court in the Thompson case continues at page 309:

“It occurs to us that a better illustration of remote and proximate cause could not be found than is furnished by the facts in the case at bar.”

“\* \* \* (In) the case at bar the alleged negligence of the employees of Cameron & Company was not the direct cause of Benton’s injuries, and could not have in any way caused Benton’s injuries except for the intervening negligence of the employees of the Railway Company.”

So also here neither could any negligence of the employees of Booth-Kelly have caused Power’s injuries “except for the intervening negligence of the employees” of the Southern Pacific Company. The negligence of Booth-Kelly, if any, was not the direct cause of Power’s injury. *Accord, Central of Georgia Ry. Co. v. Swift & Co.*, 23 Ga. App. 346, 98 S.E. 256, (unlighted shed); *Glappa v. Detroit, Etc., R. Co.*, 179 Mich. 76, 146 N.W. 134, (sand on track).



The language of the court in *Keller v. City of Fargo*, 49 N. D. 562, 192 N. W. 313, in an analogous case is helpful, for there as here one of the critical questions was what the first case (suit by injured person against the city) determined insofar as the second case (suit by city against plumber) was concerned. The court says at page 573:

“So far as Keller (indemnitor-plumber) is concerned, the judgment in the Porter case established the fact of the injury, the *physical cause of the injury*, and the effect of the injury. (Emphasis in original) *Necessarily that case determined that the city’s negligence*—that is, the breach of the city’s duty to keep the sidewalk reasonably safe—*was the proximate cause of the injury, and that judgment determined in what respect the city was thus negligent* \* \* \*

“Now the question of Keller’s negligence has become material.” (Insertion and emphasis added.)

Likewise it is submitted that here the question of the negligence of Booth-Kelly, if any, has become material. But that negligence was not decided in *Powers v. Southern Pacific Company*, any more than Keller’s was when the city was sued. but that judgment did determine in what respect the Southern Pacific was negligent, namely, in failing to warn its employee, just as city’s negligence was determined in the *Keller* case.

In the *Keller* case the court in the first action charged the jury that for the plaintiff to recover it must be

established that "the negligence of the defendant city was the proximate cause of the damage sustained." (p. 316) In *Powers v. Southern Pacific Company*, the court charged that Powers could recover only if there was negligence as charged in the complaint *and*, "second, that such negligence, if any there was, was a proximate cause of the accident." Reporter's Transcript, *Powers v. Southern Pacific Company*, p. 346.

As the passage quoted from the *Keller* case shows, the court there found from the charge given in the first action that the verdict in the first action decided that the city's negligence was the proximate cause of the injury to the pedestrian. Here, under a like charge which we have just set out, the California jury must have decided that the railroad's failure to warn was the proximate cause of Powers' injury, since the verdict was for Powers. Under the principles of res judicata and the authorities hitherto set out, the Southern Pacific Company is estopped to deny that its own negligence was the proximate cause of Powers' injury for which it now seeks indemnity.

The issue of proximate cause was thus closed by the judgment in *Powers v. Southern Pacific Company*. Furthermore as a matter of law the leaving of the cart near the track was not the proximate cause but at the most created an opportunity for the active causative

negligence of the plaintiff and its employees which this defendant was not required to foresee.

### **SPECIFICATION OF ERROR NO. III**

There is no consideration for the contract and a total lacking of mutuality for the indemnity provision contained therein. (Appellant's Appeal Point 7, T. 130)

Specifically the court below erred in making the following Findings of Fact in that there was no competent evidence to support said findings:

“There was consideration for the indemnity provisions of the spur track agreement.” (Finding of Fact No. 16, T. 54.)

### **SUMMARY OF ARGUMENT OF THE ABOVE SPECIFICATION OF ERROR**

**POINT ONE:** There was no consideration for the indemnity provision since the railroad was obliged to furnish spur track service by law in Oregon under the circumstances of this case.

**POINT TWO:** There was no consideration for the indemnity provision was inserted in revised spur track agreement by the railroad without any new consideration moving to the lumber company and after nearly forty years of operation under prior agreements without such indemnity provision.

### ARGUMENT: POINT ONE

The Southern Pacific is a "common carrier by railroad in interstate and intrastate commerce in Oregon." (Pre-Trial Order Admitted Fact, Par. I, T. 33) Nevertheless the State of Oregon may require such interstate carrier to provide spur track service. 49 U.S.C.A., sec. 1 (22), ("*Construction, etc., of spurs, switches, etc., within State.*"), specifically states of the authority of the Interstate Commerce Commission:

"The authority of the commission conferred by paragraphs (18) to (21), both inclusive, shall not extend to the construction or abandonment of spur, industrial, team, switching, or side tracks, located or to be located wholly within one State, or of street, suburban, or interurban electric railways, which are not operated as a part or parts of a general steam railroad system of transportation."

In *Texas & P. Ry. Co. v. Gulf, C. & S.F. Ry Co.*, 270 U.S. 266, 278, 45 S. Ct. 263, 70 L. Ed. 578, Justices Brandeis writing for the court said:

"When the clauses in paragraph 18 to 22 are read in the light of this congressional policy, the meaning and scope of the terms extension and industrial track become clear. The carrier was authorized by Congress to construct, without authority from the Commission, 'spur, industrial, team, switching or side tracks . . . to be located wholly within one State.' Tracks of that character are commonly constructed either to improve the facilities required by shippers already served by the carrier or to supply the facilities to others, who being within the same



territory and similarly situated are entitled to like service from the carrier. *The question whether the construction should be allowed or compelled depends largely upon local conditions which the state regulating body is peculiarly fitted to appreciate.*" (Emphasis supplied)

In *Detroit & M. Ry. Co. v. Boyne City, G. & A. R. Co.*, 286 Fed. 540, the court recognized that no certificate from the Interstate Commerce Commission was required for an intra-state spur track implying that the federal act is no bar to state regulation. The court then holds that the last clause of paragraph 22 applied only to electric railways and not to spur or industrial tracks.

In *People of State of California v. Zook*, 336 U.S. 725, 732, 69 S. Ct. 841, 93 L. Ed. 426, the court holds a specific saving of state laws by federal statutes is not essential, saying:

"That congress has specifically saved state laws in some instances, see e.g., The Securities Act of 1933, 15 U.S.C. Sec. 77R, indicates no policy save clarity."

The annotation to 49 U.S.C.A. Sec. 1 (22) in the 1949 Pocket Part is as follows:

"The exemptions contained in this section, do not necessarily reflect lack of constitutional power to deal with excepted phases of railroad enterprise, but reflect congressional policy of reserving, exclusively to the states, control over that group of essentially local activities. *City of Yonkers v. U.S.*, N.Y. 1944, 64 S. Ct. 327, 320 U.S. 685, 88 L. Ed. 400, Mandate stayed 64 S. Ct. 633."



In *New York Cent. R. Co. v. Public Utilities Commission*, 119 Ohio St. 381, 164 N.E. 427, the court held that the state commission might require reasonable service from an interstate carrier for intrastate business and that the state commission had control of intra-state spur lines. *Chicago, R.I. & P. Ry. Co. v. State*, 53 Okla. 712, 157 Pac. 1039, holds that power in the Interstate Commerce Commission to require switch connections with private side tracks where interstate business will justify the same does not deprive the Oklahoma Corporation Commission of jurisdiction to require a private switch connection where intra-state business will justify it.

Oregon has in fact exercised this power left to the states to control the construction of industrial or spur tracks. 8 O.C.L.A. sec. 113-104 provides in part that:

“All railroad shall keep and maintain adequate and suitable \* \* \* switches, spurs, and side tracks for receiving, handling, and delivering of freight transported or to be transported by such railroad.”

8 O.C.L.A. sec. 113-108 provides in substance that a shipper may require the railroad to provide a switch connection for his private track if certain requirements are met. If the railroad refuses the railroad commission is authorized to investigate and make an order requiring the connection, and such orders are to be enforceable as are any other commission orders.

“The railroad shall furnish the rails and fastenings, and the switch, complete with frog and guard

rails, and the ties and grading shall be furnished or the expense borne by applicant.” (The full text of the pertinent parts of 8 O.C.L.A. sec. 113-108 is set out in the appendix.)

Oregon has thus gone further than mere regulatory legislation; it has provided by statute that railroads must furnish spur track connections and lay such tracks.

8 O.C.L.A. sec. 113-109 is more specific than the prior sections and requires that:

“Whenever any warehouse already built or may hereafter be built within one hundred and fifty feet of the main line of any railroad in this state, with side track graded and ties laid down without expense to the company owning or operating said road, and not less than three hundred tons of freight stored in such warehouse ready for transportation, then it shall be the duty of the said railroad company to lay down the track, with the necessary connections and switches; \* \* \*”

8 O.C.L.A. sec. 113-110 provides a penalty of \$300.00 a week for each week during which the railroad’s neglect, failure, or refusal” to comply with that section (113-109) continues. (Text in appendix.)

Sections 113-109 and 113-110 were enacted together in 1885. This particular spur track was covered by agreements made on January 4, 1909 and February 27, 1909. Subsequently: (Pre-Trial Order, Admitted Facts. Paragraph II, T. 34)

“On or about June 30, 1941, the plaintiff entered

into an Industrial Track Agreement with defendant, covering the maintenance and operation of industrial track facilities serving defendant's Springfield Mill on premises used or owned by defendant, which agreement is marked pre-trial Exhibit 1."

To summarize the situation in 1945 when the injury occurred: the spur track on which the accident occurred was owned by the Southern Pacific and operated jointly by it and the lumber company. This operation was controlled by the 1941 agreement set out as Exhibit A. (T. 5). This 1941 agreement represents a revision of earlier similar agreements. Prior to any such agreements the railroad was obligated by the 1885 law to construct a spur track for the industry on the same terms on which it was in fact furnished. Just as 8 O.C.L.A. 113-109 required, in this case: (Exhibit A, Paragraph 12, T. 17)

"In the construction of said Track Railroad paid for and furnished all metal required therein and Industry paid for the ties, grading, ballast and labor."

The requirements of 8 O.C.L.A. 113-108 are similar and were also met. (Text in appendix.)

It is therefore submitted that the railroad cannot impose conditions for doing its lawful duty, laying a spur track on a prepared roadbed and operating the same. We are not here concerned with any unlawful conditions which may have been imposed by the earlier track agreements. We do strenuously object to one

illegal condition which was added to the agreement when it was rewritten in 1941, namely paragraph 7, the indemnity clause. (T. 11) Doing one's legal duty is not legal consideration. There is therefore no consideration for the various spur track agreements entered into by Booth-Kelly and in particular there is no consideration for paragraph 7 in the 1941 spur track contract requiring Booth-Kelly to indemnify the railroad.

The contention that there was no consideration for the indemnity agreement since Oregon statutes under the circumstances of this case required spur track service to be provided is not only supported by the general principles of contract law but by specific authority. The court in *Cameron v. Edgemont Investment Co.*, 149 Or. 396, 405, 41 P. 2d 249 states:

“It is the rule that a promise to pay one for doing something he was under a prior legal duty to do is not binding for want of a consideration: (Citations)”.

In *Baltimore & O.S.W.R. Co. v. Cincinnati, L. & A.E. St. R. Co.*, 52 Ind. App. 639, 99 N.E. 1018, the court held a contract to pay a watchman imposed on a street railroad desiring to cross a steam railroad's track was unenforceable for lack of consideration since the street railroad had a right to cross over the steam road's tracks subject to no conditions except those imposed on the general public. The court says at page 643:

“\* \* \* (In) other words, the consideration for ap-



appellee's promise was the consent of appellant to cross at grade its track on Walnut street.

"If appellee acquired some legal right, or any legal possibility of benefit by its promise, a sufficient consideration would be shown, but the mere consent or withdrawal of an objection by appellant to the doing of that which appellee had a legal right to do, is not a consideration sufficient to support a promise. This is so on the theory that the promisor gets nothing in return for his promise but that to which he is legally entitled. (citations)"

The *Baltimore* case was followed in two cases which hold that the giving by a railroad of a privilege that it was obligated to give as a matter of law was not consideration for imposing contractual duties on another party. *Vandalia R. Co. v. Ft. Wayne & Northern Indiana T. Co.*, 68 Ind. App. 120, 118 N.E. 839, *Terre Haute, I. & W. Traction Co. v. Ross*, 84 Ind. App. 697, 138 N.E. 90.

To like effect that performance of a legal duty by a railroad is not consideration for a contract with another party the holding in *The Kansas City, St. J. & C. B. Ry. Co. v. Morley*, 45 Mo. App. 304, Headnote 2 is as follows:

"2. **Contracts:** CONSIDERATION. A contract between a city contractor for the construction of a sewer along a street and a railway company having a right of way over such street, that the contractor would pay the company for supporting its tracks while he built the sewer is a *nudum pactum*,—without consideration,—and void."

In *South & North Ala. R. R. Co. v. Highland Ave. & Belt*



*R. R. Co.*, 119 Ala. 105, 24 So. 114, the question was the specific performance of an agreement allowing a belt line railroad to cross another railroad. The court in dealing with the consideration necessary to make a contract entitled to such relief said:

“Of the other matters, agreed to be performed by the Elyton Company, some were such as statutes in force at that time required it to perform, and therefore constituted no valid consideration, such as the giving to defendant or preferential rights at the crossing.—Code, Sec. 1145.”

Finally the opinion of Judge Learned Hand in *China Fire Ins. Co. v. Davis*, 50 F. 2d 389, 76 A.L.R. 1259, *cert. denied* 284 U.S. 658, 52 S. Ct. 36, 76 L. Ed. 558, is an analogous authority which suggests the rule of law which ought to be controlling here. A clause in a bill of lading giving a carrier railroad the benefit of any insurance carried on a shipment was held invalid under 49 U.S.C.A. sec. 2:

“as giving carrier greater compensation than collected for similar service.” (Headnote P. 389) (Text in appendix)

Here Booth-Kelly pays the regular rate for shipping lumber, it would then seem that the indemnity clause is additional prohibited compensation over that paid by other lumber shippers. Furthermore if the legal rate is paid that is full consideration for any services the rail-

road may render; it then follows that to impose an indemnity agreement on the shipper lacks consideration since he has already paid the maximum rate legally possible for the services rendered.

In summary our argument is that the Interstate Commerce Act leaves to the states the regulation of spur tracks located wholly within one state. The track here was such a track and Oregon by statute has made specific provision to force railroads to construct and maintain spur tracks for shippers under certain conditions. Those conditions of grading and laying down the ties were met in this case. Since the Southern Pacific Company was obliged as a matter of law to furnish the spur track and service thereon, no consideration moved to Booth-Kelly for the indemnity clause imposed by the railroad's form contract and on which it now relies.

We have cited authority establishing that in analogous cases where a track or a sewer had to cross an existing railroad line that such lines could not impose contractual conditions on the constructing party where such constructing party had the legal right to cross the existing line. Secondly we have cited *China Fire Ins. Co. v. Davis, supra*, to establish that under the Interstate Commerce Act such indemnity agreement is without consideration since the freight and switching rates charged by the railroad are full lawful consideration

for spur track service. In addition the indemnity agreement is itself an unlawful attempt to impose a discriminatory rate upon Booth-Kelly.

Several subsidiary questions of law remain to be considered. First the state cases hitherto cited on consideration by implication affirm that such relationships as in providing spur tracks are statutory rather than contractual. We cite the following cases as direct authority for that proposition:

In *Chicago, R. I. & P. Ry. Co. v. State, supra*, the court sustained by implication a constitutional provision requiring switch connection to be made by the railroad in much the same way as 8 O.C.L.A. sec. 113-108 summarized above does. (Text set out in appendix.) In that case a contract to construct a side track had been breached. The court held:

“The jurisdiction of the commission under this provision to require a switch connection to be made is not founded upon any contractual relation between the parties, nor does it arise by reason of the alleged breach of a contract to construct such switch, but it depends upon the existence of a state of facts which brings the case within the terms of said constitutional provision.” (P. 721)

Likewise it is our contention that here the construction of a spur track was pursuant to Booth-Kelly's right under the Oregon statute and did not depend on any contractual relationship between Booth-Kelly and the railroad.

In *New York Cent. R. Co. v. Public Utilities Commission of Ohio*, 119 Ohio St. 381, 387, 164 N.E. 427, the court said:

“The application for the order was for intrastate service. The Public Utilities Commission of Ohio has jurisdiction of intrastate service and over spurs and switches. The fact that the rendering of service by the common carrier may create a liability growing out of a contract does not operate to deprive such commission of jurisdiction to require service.”

In *Portland Terminal Co. v. Boston & M. R. R.*, 127 Me. 428, 144 A. 390, a Maine law allowed a terminal company to be set up. Each railroad company was to pay for the use of the terminal:

“\* \* \* in the proportion in which it has the use thereof, the same to be fixed by the *written agreement* of all such railroad companies \* \* \*” (P. 430) (Emphasis supplied)

In case they failed to agree a statutory procedure was provided.

The court said at page 438:

“This provision for fixing of proportionate payments does not, we think, sound in contract. It creates no legal liability on the part of one railroad to the other, or by either to the Terminal Company, which can be enforced under the law of contract. It provides for a mutual ‘expression of assent’ enforceable only under the special jurisdiction conferred upon the court of equity by the Act. The statute creates the right and gives the remedy which is appropriate and therefore exclusive. (citations)”

Likewise in this case whatever contracts the parties may have entered into in relation to the provision of a spur track create no legal liability which can be enforced under the law of contracts. There the difficulty was a special equity enforcement procedure; here one difficulty is a lack of consideration since the railroad is obliged by Oregon statutes to furnish spur track service under the conditions here existing. Furthermore under the Oregon statute the remedy of the shipper is not under contract law just as is also true in the *Boston & M. R. R.* case. 8 O.C.L.A. 113-108 provides for shipper securing an administrative order from the railroad commission for service and 8 O.C.L.A. 113-110 provides for a statutory penalty of \$300.00 per week which the warehouse owner may recover from the railroad.

To summarize, in both the instant and *Boston & M. R. R.* cases the parties contracted but in neither case did the agreements sound in contract. In both cases the statutory remedies are exclusive. Under this view, the purpose of the agreement here is as was said of the agreement required there:

“\* \* \* to prevent uncertainty, to perpetuate evidence, and create a memorial which permits of no doubt or uncertainty, it was the legislative intent that the agreement be written as to all the railroads, be intended as an ‘expression of assent’ and possess some degree of formality.”



It lacks any legal effect because there was no consideration.

Both the *Chicago* and *Boston & M. R. R.* cases are authority for the proposition that the relationships are here statutory rather than consensual. Since the relationship is statutory and the railroad is obliged to furnish spur track service by statute there was no consideration moving to Booth-Kelly for any agreements it signed.

The second subsidiary question of law to be considered is the authority of the Oregon Legislature to pass the above cited statutes on spur tracks. In *Southern Pac. Co. v. Railroad Commission*, 60 Or. 400, 119 Pac. 727, the court held that the commission might order a spur track constructed under statutes then existing. One of the sections there relied on was Section 6897, L.O.L.; that section became 8 O.C.L.A. Sec. 113-104 in subsequent codifications and we have set it out above. Objections were made to the spur track order upon the ground of the Fourteenth Amendment to the United States Constitution, but the court held that the order was not contrary to the amendment.

In *Chicago & N. W. Ry. Co. v. Ochs*, 249 U.S. 416, 39 S. Ct. 343, 63 L. Ed. 697, the court sustained a state law under which the state commission had assessed two-thirds of the cost of a spur track against the railroad and one-third against the shipper. Here the track also has a

public character since paragraph 4 of the agreement allows the railroad to use said track in service of others and to have control of the track in general. (T. 8) And in fact at the time of the accident the railroad was engaged in such public use serving other shippers on the same track. (T. 90) The *Chicago & N. W. Ry.* case was followed in its companion case, *Lake Erie & W. R. R. Co. v. Pub. Util. Comm.*, 249 U.S. 422, 39 S. Ct. 345, 63 L. Ed. 684,

“as to the power of a state to require a railroad company at its own expense to restore a siding, used principally by a particular plant but available generally as a public track, owned and controlled by the railroad as part of its system. P. 424.”

“Such a requirement does not take the Company’s property for private use, or for public use without compensation, in contravention of the fourteenth Amendment. P. 425” (Headnote)

The question of the power of the state to compel a railroad to build, maintain, or connect with sidetrack for the accommodation of shippers is recognized and annotated in L.R.A. 1918B, page 786.

### **ARGUMENT: POINT TWO**

Oregon follows the general contract rule

“that a modification of a contract being a new contract, a consideration is necessary to support the new agreement, as, for example, where to extend the time for performance or payment or to release

one of the parties from performance.” *Cameron v. Edgemont Investment Co.*, 149 Or. 396, 402, 41 P. (2d) 249.

As has been pointed out,

“On or about June 30, 1941, the plaintiff entered into an Industrial Track Agreement with defendant, covering the maintenance and operation of industrial track facilities serving defendant’s Springfield Mill on premises used or owned by defendant, which agreement is marked pre-trial Exhibit 1.” (Pre-trial Order, Admitted Facts, Par. 2, T. 34.)

That agreement is printed as Exhibit A in the record of this case. (T. 5) According to paragraph 20 of that contract, the

“agreements of January 4, 1909 and February 27, 1909 are hereby terminated as of the date hereof.” (T. 19)

These prior agreements did not contain any indemnity clause such as was incorporated in the present agreement as paragraph 7. (T. 11) That particular paragraph of the agreement, and in fact the whole first ten paragraphs in the agreement, were part of printed form contract provided by the railroad and imposed upon the shipper.

Even if it be assumed that there was consideration for the superseded agreements of 1908 and 1909, there was no consideration moving to Booth-Kelly for modifying the agreement to accept liability under a new gen-

eral indemnity provision. The printed indemnity clause of the form contract was inserted without any special attention being called to it under the guise of modernizing the ownership situation.

In summary, no new consideration moved to Booth-Kelly. Despite this fact the Southern Pacific as part of the process of rewriting the contract inserted as part of the new contract a printed form which contained a standardized indemnity clause. It is upon this printed form paragraph that recovery was had in the court below; this was error since there was no consideration moving to this defendant for that added liability.

#### **SPECIFICATION OF ERROR IV**

The contract has no application because the indemnity provision thereof, namely Paragraph VII, is applicable only when railroad (Appellee) is serving industry and at the time of the accident railroad (Appellee) was not serving industry. (Appellant's Appeal Point 8, T. 130)

Specifically the court below erred as a matter of law in construing the indemnity clause (Paragraph 7) of the contract to cover operations on the track when the railroad was not serving Booth-Kelly, with result that it erroneously made and entered the following Conclusion of Law:

“Plaintiff is entitled to recover judgment against defendant for the sum of \$22,000.00 *on the contract*,

together with its costs and disbursements incurred herein.” (Emphasis supplied) (Conclusion of Law No. 7. T. 55)

**POINT ONE: Applying the usual constructional rules in this business context, the “serving industry” requirement applies to both sentences of Paragraph 7 with the result that the indemnity provision was in-operative under the circumstances here.**

### **ARGUMENT: POINT ONE**

Here the whole purpose of the agreement was to supply spur track service to Booth-Kelly for the mutual benefit of the two parties. As a concession to the railroad it was granted “the right to use the (track) when not to the detriment of Industry.” (T. 8) Now the railroad is forced to contend that since the second sentence of Paragraph 7 does not repeat the serving industry clause, that Booth-Kelly is obliged to indemnify the railroad even if the railroad is engaged in serving other persons as it was here. (T. 90)

Paragraph 7 of the spur track agreement contains only two sentences: first, an indemnity agreement by Industry against its own losses and losses of the property of others on its premises arising from fires caused by the Railroad’s locomotives; second, a sentence in which Industry agrees to indemnify the railroad for loss caused by Industry’s negligence, or by the joint



negligence of the parties. (T. 11) The first sentence is specifically restricted to cases where the Railroad is operating:

“on said track, or in its vicinity, for the purpose of serving said Industry \* \* \*” (T. 11)

It is submitted that this serving Industry phrase also modifies the second sentence which is the basis of this litigation. The second sentence is closely related to the first sentence; its introductory words being “Industry also agrees \* \* \*.”

In Oregon it is settled that:

“\* \* \* the punctuation of an act or its title is not controlling in construing it for the purpose of ascertaining its real meaning.” *State ex. rel. v. Banfield*, 43 Or. 287, 291, 72 Pac. 1093.

The same principle is applied elsewhere to contracts. *Stoddard v. Golden*, 179 Cal. 663, 178 Pac. 707, 3 A.L.R. 1060 and the annotation thereto. Furthermore Oregon, in its statutes, treats the construction of statutes and instruments in the same sections as similar problems; for example, 1 O.C.L.A. 2-217 provides:

“In the construction of a statute the intention of the legislature, and in the construction of an instrument the intent of the parties is to be pursued, if possible \* \* \*.”

Therefore since punctuation of a contract is not controlling as to its meaning no more should paragraphing.

Here the drafter made each sentence on indemnity a separate paragraph but still lumped them under a single number, seven. We contend that the two sentences on indemnity so lumped under one number should be construed as one paragraph, with the result that the second sentence is modified by the words while "serving said Industry." If that clause so modifies the second sentence which is in litigation here, that second sentence can have no application because at the time the accident occurred the railroad was not serving Industry. (T. 90)

Even if the two sentences do not constitute one paragraph, the general principles of contract law require that the condition of serving industry be attached to the second sentence providing indemnity against the railroad's joint negligence. First,

"The intention of the parties must be determined from a consideration of the entire instrument, and not of detached portions thereof. (Citations)" *Champion et. ux. v. Hammer et. ux.*, 178 Or. 595, 604, 169 P. (2d) 119.

It is thus clear that the second sentence should not be considered apart from the serving industry clause in the first sentence.

The court in the *Champion* case continues at page 605 with another rule of construction helpful here:

“When clauses in a contract are repugnant and incompatible, the general rule of construction is that, unless the inconsistency is so great as to avoid the instrument for uncertainty, the earlier clause prevails. (Citations)”

The two sentences here are inconsistent if the serving industry clause applies only to the sentence in which it happens to have been placed. It is inconsistent that the parties should have agreed that Booth-Kelly was to indemnify the railroad against locomotive fire damage *only* when the railroad was serving Booth-Kelly and then in the next succeeding sentence agree it was to indemnify the railroad for losses incurred in the use of the spur track even if the railroad was serving other customers as it was here and as it had the right under the contract to do. (T. 90, 8) Under the rule of construction announced since the sentences do impose inconsistent obligations on Booth-Kelly, the earlier sentence containing the serving industry clause should prevail.

The third rule of construction favoring the interpretation that the serving industry clause modifies the second sentence is the rule that a contract is construed against its preparer particularly if it is a printed form contract. This principle has been particularly applied to form insurance contracts; it is submitted that it is no less applicable to the indemnity clause of a form spur track agreement. Here the whole of Paragraph 7 is in-

cluded in that part of the contract for which the railroad used one of its standard printed forms. The words of the Oregon court in *Keeler Bros. v. School District No. 108*, 91 Or. 316, 324, 178 Pac. 218, are substantially applicable here:

“The plaintiff is an expert in the matter of contracts like this. It prepared the contract itself and in its own language. It deals with the officers of a school district, who are ordinarily inexperienced in such matters. We think it should be held strictly to each provision of its contract, and if there is any vagueness in the contract which it itself, has prepared, that vagueness should be construed against it rather than in its favor.”

Here the railroad had it within its power to make it clear that the second sentence was not modified by the serving industry clause in the first sentence of Paragraph 7, but it failed to do so.

The fourth rule of construction favoring the interpretation that the serving industry clause modifies the second sentence is:

“\* \* \* the settled rule of construction that, where a contract is susceptible of different interpretations, or more of which would enable it to stand, and others which might vitiate the instrument, the construction giving effect to all its parts, and sustaining the contract and carrying out the evident intention of the parties thereto, will prevail, rather than the construction nullifying the instrument: (citations)” *Olympia Bottling Works v. Olympia Brewing Co.*, 56 Or. 87, 99, 107 Pac. 969.

Specifically if the serving industry clause does not modify the second sentence the second sentence cannot stand because there is a lack of consideration for Booth-Kelly to indemnify the railroad for damage jointly caused by the railroad while serving someone else. Furthermore,

“It is a well-established rule of law that courts should incline, where such a construction is reasonable, to construe a contract in favor of mutuality: (citations)” *Ward v. McKinley*, 97 Or. 45, 54, 191 Pac. 322.

The only possible consideration for Booth-Kelly agreeing to the spur track contract was spur track service. We do not concede that such was consideration under the circumstances of this case, but even if it was consideration it is clear that no consideration moves to Booth-Kelly for its continuing obligations when the railroad was not in fact serving Booth-Kelly. It was not serving Booth-Kelly here. (T. 90)

In summary, the serving industry clause should be construed to modify the second sentence as well as the first sentence in Paragraph 7 of the agreement because first, they constitute a single paragraph, and second, four settled rules of construction require it: (1) construe the instrument as a whole, (2) in case of inconsistency the earlier clause prevails, (3) a contract is construed against its preparer especially if it is a printed form contract, and (4) construe to sustain the instru-



ment, specifically here construe to avoid a lack of mutuality; and, third, the purpose of the agreement was only to serve Booth-Kelly.

### **SPECIFICATION OF ERROR NO. V**

No recovery can be allowed Appellee under the contract as it is an attempt to contract against its own negligence, the contract is void as against public policy under the laws of the State of Oregon as otherwise it would permit Appellee to recover for a loss it sustained through its own negligence. (Appellant's Appeal Point 5, T. 129)

Specifically the court below erred as a matter of law in holding by implication that the indemnity clause (Paragraph 7) of the contract was a valid contract with the result that it erroneously made and entered the following Conclusion of Law:

“Plaintiff is entitled to recover judgment against defendant for the sum of \$22,000.00 *on the contract*, together with its costs and disbursements incurred herein.” (Emphasis supplied) (Conclusion of Law No. 7, T. 55)

### **SUMMARY OF THE ARGUMENT OF THE ABOVE SPECIFICATION OF ERROR**

**POINT ONE:** Under the doctrine of **ERIE RAILROAD CO. V. TOMPKINS** as presently interpreted, a dictum of the Oregon court that an agreement to indemnify an indemnitee against his own negligence is

against public policy settles the law of Oregon for this case.

**POINT TWO:** Irrespective of any Oregon authority, the general rule is that an agreement to indemnify an indemnitee against his own negligence is contrary to public policy.

### **ARGUMENT: POINT ONE**

Paragraph 7 of the spur contract provides in part that:

“\* \* \* if any claim or liability, other than from fire, shall arise from the joint or concurring negligence of both parties hereto, it shall be borne by them equally.” (T. 12)

Obviously if this clause is valid under Oregon law the railroad is permitted to recover from the indemnitor Booth-Kelly for the railroad's own negligence.

The question here is then quite simple: is it against the public policy of Oregon for the railroad to enter into a contract to be indemnified against the consequences of its own negligence? The question has not yet been decided in Oregon; yet the Oregon court has unequivocally indicated what it considers to be the law.

In *Southern Pacific Co. v. Layman*, 173 Or. 275, 278, 145 P. 2d 295, the railroad sought to recover on an indemnity clause in a printed form contract allowing the defendant to construct and use a private road crossing

upon the defendant's right of way. The court says at page 278:

"The question for decision is whether the indemnity clause covers a case of loss suffered by the plaintiff solely as the result of its own negligence in the operation of one of its trains.

"We do not stop to inquire whether the agreement, if so construed, would be valid. That question has not been raised, although, *according to the editors of American Jurisprudence, a majority of the American courts hold that an agreement to indemnify against the negligence of the indemnitee is void as against public policy*: 27 Am. Jur., Indemnity 460, sec. 9." (Emphasis supplied)

The Layman case is a recent one, having been decided in 1944, and the judge's assertion is no casual remark of his own but a statement of the general rule backed by authorities.

The basic problem is the weight which this court will accord to this considered *dictum*. Even before the Supreme Court decided *Erie Railroad Co. v. Tompkins*, 304 U.S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, this court said in *Collins v. Streitz*, 95 F. 2d 430, 435, *cert. denied* 305 U.S. 608, 59 S. Ct. 67, 83 L. Ed. 388, discussing a similar problem:

"The other Arizona case discussing acknowledgments is *Larkin v. Hagan*, 1912, 14 Ariz. 63, 126 P. 268, 272 rehearing denied July 15, 1912. The language therein contained bearing on the sufficiency of the acknowledgment involved is expressly stated to be unnecessary to the decision. However, in view

of the paucity of authority on the point, it is entitled to great weight. (Citations)”

Since the Erie decision this court affirmed a decision of the Oregon District Court, (133 F. 2d 160) in the case of *American Surety Co. v. Bank of California*, 44 F. Supp. 81. The district court says:

“These (sic) is no binding authority in the state of Oregon upon the exact situation here presented. Many authorities have been cited from other jurisdictions. But calculation of numerical weight of authority from other jurisdictions will not suffice. This court must attempt to give weight to the considerations which, judged from previous utterances, will affect the Supreme Court of Oregon, when that tribunal deals with a state of facts such as is here presented.” (P. 83)

He continues at page 87:

“If the Oregon courts were confronted with the facts here involved, it is believed the principles announced in the last quoted case (*American Central Insurance Company v. Weller*, 106 Or. 494, 212 Pac. 803) would be followed.” (Citation inserted)

This court said of the Weller case in its opinion on the appeal:

“Admittedly, the facts vary widely from those in the instant case, but the court’s limitation of the subrogation doctrine is significant.” (P. 164)

Under the Erie case “the rules of decision established by judicial decisions of state courts are ‘laws’ as well as those prescribed by statute.” *West v.*

*American Telephone & Telegraph Co.*, 311 U.S. 223, 236, 61 S. Ct. 179, 85 L. Ed. 139.

The court in the *West* case continues at page 236:

“There are many rules of decision commonly accepted and acted upon by the bar and inferior courts which are nevertheless laws of the state although the highest court of the state has never passed upon them. \* \* \* State law is to be applied in the federal as well as the state courts and it is the duty of the former in every case to ascertain from all the available data what the state law is and apply it rather than to prescribe a different rule, \* \* \*”

Justice Stone's words of course refer to a failure to conform to the decision of an inferior state court, but their logic is equally applicable here.

His statement that “all the available data” as to what is state law has been followed and applied in many cases; one of which is *Yoder v. Nu-Enamel Corporation*, 117 F. (2d). The Eighth Circuit said at page 489:

“And the obligation to accept local interpretation extends not merely to definite decisions, *but to considered dicta as well*. *Hawks v. Hamill*, 288 U. S. 52, 53 S. Ct. 240, 77 L. Ed. 610; *Badger v. Hoidale*, 8 Cir., 88 F. 2d 208, 109 A.L.R. 798. Indeed, under the implications of *Erie Railroad Co. v. Tompkins*, 304 U.S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, 114 A.L.R. 1487, and *West v. American Telephone and Telegraph Co.*, 61 S. Ct. 179, 85 L. Ed. ....., where direct expression by an authorized state tribunal is lacking, it is the duty of the federal court, in dealing with matters of either common law or statute, to have regard for any per-



suasive data that is available, such as compelling inferences or logical implications from other related adjudications and considered pronouncements. The responsibility of the federal courts, in matters of local law, is not to formulate the legal mind of the state, but merely to ascertain and apply it. Any convincing manifestation of local law, having a clear root in judicial conscience and responsibility, whether resting in direct expression or obvious implication and inference, should accordingly be given appropriate heed." (emphasis supplied)

In *Stentor Electric Mfg. Co. v. Klaxon Co.*, 125 F. 2d 820, *rev'd on other grounds* 313 U.S. 487, 61 S. Ct. 1020, 85 L. Ed. 1477, the Third Circuit went further in applying the *West* doctrine of use of all available data than in simply following a dictum. The court said at page 824 that the state court's proneness to use the Restatement should be considered:

"Among the items of data available is the approach of the Delaware Supreme Court to this kind of problem in the Nelson case. \* \* \* It did not have previously decided Delaware cases to settle the point. It examined and cited cases from other states, three current textbooks in the Conflict of Laws and the Restatement. It accepted and applied what was set forth in these sources. This seems to us strong evidence of what the Delaware court would do in a conflict of laws problem, and the case gains additional strength from the fact that it was recently decided."

Recently the same principle has been applied with a federal court noticing that:

“\* \* \* Delaware courts pay particular attention to the decisions of the Courts of Massachusetts.” *Wilmington Trust Co. v. Mutual Life Insurance Co.*, 76 F. Supp. 560, 565.

If these courts go so far as to ascertain the state law, it would seem *a fortiori* that a considered dictum like the one here should be followed.

This continuing expansion of the Erie doctrine to include state court's recognition of rules of laws seems to be endorsed by the Supreme Court in a footnote to *Shelly v. Kraemer*, 334 U.S. 1, 17, 68 S. Ct. 836, 92 L. Ed. 1161:

“In applying the rule of *Erie R. Co. v. Tompkins*, 1938, 304 U.S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, 144 A.L.R. 1487, it is clear that the common-law rules enunciated by state courts in judicial opinions are to be regarded as a part of the law of the State.”

Similarly the following circuit court decisions indicate a like trend. The Fifth Circuit said in *Meredith v. Board of Public Instruction*, 112 F. 2d 914, 916, *cert. denied*, 314 U.S. 656, 62 Ct. 109, 86 L. Ed. 526:

“When that court has not ruled upon the precise question involved, we apply the law as we understand it to be in that state.”

The Sixth Circuit said in *Princess Garment Co. v. Fireman's Fund Ins. Co.*, 115 F. 2d 380, 383:

“The Supreme Court of the State of Ohio has not yet passed directly upon the questions here present-

ed and we have applied the rule that this court will exercise an independent judgment in determining the law with respect to the issues here presented based upon whatever principles of state law are applicable.”

Finally the Third Circuit in *Jackman v. Equitable Life Assur. Soc.*, 145 F. 2d 945, 947, said:

“In order to apply local law where there is no authoritative local decision or statute, it is incumbent upon a federal court to ascertain and apply what it believes to be the law which a court, authorized to speak the law of the particular State, would apply if called upon to adjudicate upon like circumstances.”

In summary, Paragraph 7 of the spur track agreement seeks to indemnify the railroad against its own negligence. We contend that such an agreement is contrary to public policy in Oregon; and the Oregon court has asserted that the general rule is that such agreements are void in order to avoid any suggestion that it was accepting by inference the validity of such agreement in *Southern Pacific Company v. Layman, supra*. Under the doctrine of *Erie Railroad Co. v. Tompkins, supra*, as presently applied by the Supreme and Circuit Courts such a considered pronouncement as to the general law must be followed in this case since it clearly indicates what the Oregon court conceives to be the law. Even apart from *Erie Railroad v. Tompkins, supra*, the federal courts are required to follow state law on this

subject matter since it was expressly left to the states by the Interstate Commerce Act previously set out and by case law generally apart from any statute. *Hartford Ins. Co. v. Chicago & C. Railway*, 175 U.S. 91, 20 S. Ct. 33, 44, L. Ed. 84.

### ARGUMENT: POINT TWO

If this court does not deem itself bound by the Layman dictum as to the Oregon law on indemnity against one's own negligence, the contract here sued upon is void as against public policy by the general rule.

Many cases so hold:

*Nashua Gummed & Coated Paper Co. v. Noyes Buick Co.*, 93 N.H. 348, 41 A. 2d 920.

*Otis Co. v. Maryland Co.*, 95 Colo. 99, 33 P. 2d 974.

*Johnson's Admx. v. Richmond & D. R. Co.*, 86 Va. 975, 11 S.E. 829.

*Accord: Wessman v. Railroad*, 84 N.H. 475, 162 A. 476.

*Fairfax Gas & Supply Co. v. Hadary*, 151 F. 2d 939.

*City of Gary v. Bontrager Const. Co.*, 113 Ind. App. 151, 160, 47 N.E. 2d 182.

*See: Jankele v. Texas Co.*, 88 Utah, 325, 329, 65 P. 2d 425.

*City of Phila. v. The Phila. Gas Works Co.*, 49 D. & C. (Pa.) 314, 322.

**SPECIFICATION OF ERROR NO. VI**

There was no breach of contract. Appellee's loss did not result through breach by Appellant of the contract. Any breach of the contract was fully known to Appellee and was waived by it. (Appellant's Appeal Point 1, T. 128.)

Appellee is estopped by its conduct from asserting that alleged breach of contract caused its loss as a custom of operation had been developed between the parties covering the removal of any obstruction to track clearance upon request of Appellee. (Appellant's Appeal Point 2, a, T. 128-9.)

The claimed breach of clearance was discovered by Appellee long prior to damage and therefore such damage was not caused by the claimed breach. (Appellant's Appeal Point 2, b, T. 129.)

The above points raise questions which are substantially alike and in the interests of brevity and convenience the three above points are consolidated and treated as a single specification of error.

Specifically the court below erred in making the following Findings of Fact since there was no evidence to support them:

"The placing and leaving of the wood cart within 42 inches from the track was a breach of the provisions of said agreement relating to impaired clearances." (Finding of Fact No. 21, T. 54.)

"The damage to Powers and the liability of plaintiff was the natural or necessary result of defendant's breach of contract." (Finding of Fact No. 13, T. 53-54.)



“There was no custom or practice between the parties under which plaintiff would give notice to defendant of any objectionable obstruction to track clearance or of defendant moving the same at the request of the plaintiff.” (Finding of Fact No. 19, T. 54.)

The court below further erred as a matter of law in making and entering the following conclusion of law:

“Plaintiff did not waive defendant’s breach of contract.” (Conclusion of Law No. 3, T. 55.)

### **SUMMARY OF THE ARGUMENT OF THE ABOVE SPECIFICATION OF ERROR**

**POINT ONE:** There was no breach of the spur track contract relating to clearance.

**POINT TWO:** If there was a breach, appellee’s loss did not result from alleged breach.

**POINT THREE:** If there was a breach, appellee can claim no benefit thereby since he waived any breach and in any case was estopped by the custom of the parties as to the removal of any obstruction.

### **ARGUMENT: POINT ONE**

Paragraph 5 of the agreement is in part as follows:

“Industry agrees that without the written consent of Railroad first had and obtained, no structure, material, pole, cable, wire, conduit, pipe, opening, excavation or obstruction of any character shall be erected, piled, made, stored or maintained upon or over the premises of Railroad, or beneath any track

upon the premises of Railroad. In the event such written consent is given, Industry agrees to comply with the following minimum clearances: . . .” (T. 8)

As is evident the words refer to such things as structures and pipes. The only possible way an iron-wheeled wood cart could be covered is by the catch-all phrase: “obstruction of any character.” By the application of the familiar principle of *eiusdem generis*, the particular words like structure, pipe, and excavation control the meaning to be attributed to the general word “obstruction.” *Smith v. First Nat. Bank*, 114 Okla. 293, 245 Pac. 653. These words uniformly refer to fixed objects or to objects which if they move, move in a very limited range. Doors, windows, and gates, objects which are customarily movable are treated specially later on in the paragraph, but not wood carts so the inference is that they are not covered by the agreement. This inference is strengthened by the requirement that written permission is to be obtained for maintaining such on the premises of the railroad. It is hardly likely that the lumber company was to get permission if a “hyster” was moved onto the railroad’s premises to load a freight car. Here the “obstruction” was a movable vehicle, a wood cart, and it is no less tenuous to claim that written consent must be obtained to move it onto the railroad premises adjacent to the mill. And it is only if written

consent is given (required) that Industry agreed to comply with the stated minimum clearances.

### ARGUMENT: POINT TWO

We have previously argued, Specification of Error No. II, point two, that leaving the cart near the tracks was not the proximate cause of the damage to Powers and the consequent liability of the plaintiff the argument here is substantially the same and that section will not be repeated. It should be noted that the only breach alleged is the leaving of the wood cart near the tracks. Merely creating a condition in which the negligence of others may be effective does not amount to proximate causation since this defendant is not required to anticipate the negligence of the railroad. *Wm. Cameron & Co. v. Thompson*, ..... Tex. Civ. App. ...., 175 S.W. 2d 307 (unblocked hand truck rolling out of freight car). In *Central of Georgia Ry. Co. v. Swift & Co.*, 23 Ga. App. 346, 98 S.E. 256, the court, where the railroad had failed to warn an employee of a danger or to light it, held:

“The act of the railroad company in thus voluntarily operating its train along said private track and under said shed, and in such undisproved negligent manner did not amount to mere legal, passive acquiescence in the negligence of the oil company in maintaining the shed in a dangerous condition, but such active, positive and negligent conduct on the part of the railroad itself amounted to an actual participation by it in the *proximate* cause of the homicide.” (Emphasis supplied)

In *Glappa v. Detroit, etc., R. Co.* 179 Mich. 76, 80, the court in speaking of sand on a private side track which the industry served had contracted to remove said:

“If the cars had not been moved, the plaintiff would not have been injured. It was the alleged negligent movement of the cars over the accumulated sand which caused the injury.”

So here it was the movement of the cars which caused the injury not the cart being left within 42 inches of the track.

Furthermore the movement of the cars was negligent here. The finding of the court that:

“Employees of plaintiff observed the position of the cart and operations continued thereafter prior to the accident.” (T. 54)

is well substantiated. Both the conductor and engineer testified that they noticed the cart three or four days prior to the accident having been in there several times in that period (Reporter's Transcript, *Powers v. Southern Pacific*, P. 20, 83-4). The fireman also saw it several times and in fact when he first saw it had warned the engineer but the engineer on the basis of his previous experience indicated he would clear it. The fireman knew that he noticed this on January 30th the first day he had returned to work. (Reporter's Transcript, P. 88-89.)

The accident happened on February 8th, so both



the engineer and fireman had known about the obstruction for at least 8 days. The other brakeman noticed the cart on the way in with the train load of logs. (Reporter's Transcript, P. 80.) Counsel for the Southern Pacific in the Powers case stated in his argument to the jury:

"It has been an admitted fact all the way along, that the wood cart was there three or four days. One witness said from January 30th, but every member of that crew knew, except Mr. Powers. \* \* \*

"Mr. Powers had been in the Booth-Kelly plant as much as anybody else on that crew, and that crew worked regularly. One witness said he remembers distinctly going in the day before. Another witness said two or three days before. We know they were in there on the 30th. We know that they were in there pretty regularly, \* \* \*" (Reporter's Transcript, P. 283-4.)

He continued:

"These men in the crew, if they knew it was in there—and they all knew, all of them,—if they thought they were going to get hurt, they could have refused to switch. They did not have to go in if they thought it was as dangerous as all that.

"But they all knew it was there, that is the fact, and all knowing that it was there, they went on in, and there was plenty of room, the engineer told you that." (Reporter's Transcript, P. 306.)

This particular train was in charge of a conductor. (T. 34) Despite this and the knowledge of every other member of the crew, Powers was not warned of the location of the cart. (Reporter's Transcript P. 130) Furthermore Powers was descending backwards from the



car when struck (Reporter's Transcript P. 165) yet counsel for the railroad stipulated:

"No signs were posted in or on the caboose regarding the manner of detraining." (T. 109)

Neither the conductor nor the railroad gave any notice that the clearance was impaired as is required by company rules:

"Rule 1094, Rules and Regulations of Maintenance of Way and Structures, Southern Pacific Company, Pacific Lines, dated November 15, 1943: (set out in part)

"Where occupants of company property under lease encroach upon standard clearances with buildings, lumber, coal piles or other obstructions, they must be courteously notified to comply with standards." (Reporter's Transcript, Pp. 21-22.)

Finally to switch on an obstructed track is itself negligent if the railroad employees know of the obstruction. In *Kanawha Railway v. Kerse*, 239 U.S. 576, 579, 36 S. Ct. 174, 60 L. Ed. 448, the court said of a switch track obstructed by a board across the track approximately 3 to 4½ feet above the top of a box car:

"The action of the Railway Company through its employees, in conducting its switching operations upon a switch obstructed, as this one was, in such manner as to endanger the lives of brakemen upon its cars, speaks so clearly of negligence that no time need be spent upon it. The evidence that the timber had been in the position described for a considerable period of time was presumptive evidence of notice to the company; besides which, the switch engineer

and conductor both testified to actual knowledge on their part, prior to the time of the accident to Barry."

In summary it is clear that the Southern Pacific loss did not result from any breach of the contract in leaving the cart near the track since the railroad knew of such condition and failed to warn its employee and also persisted in switching on this obstructed track which operation is itself negligence.

### **ARGUMENT: POINT THREE**

The knowledge of the railroad's employees, and in particular, of the conductor in charge of the crew repeatedly using this switch despite its obstruction constituted a waiver of any breach of the contract. In *Cross v. Campbell*, 173 Or. 477, 493, 146 P. 2d 83, the court states:

"It is axiomatic that a party to a contract may waive performance of any of its provisions if he so chooses."

In *Smith v. Martin*, 94 Or. 132, 138, 185 Pac. 236, the court considered waiver of a non-assignability provision in a contract and stated:

"Such waiver may be proved by parol and by circumstantial evidence, as well as by direct testimony."

Here parol and circumstantial evidence shows a waiver.

The court continues in the Martin case:

“ ‘Waiver’ is a voluntary relinquishment of one’s known right, and may be by the acts of the party \* \* \* ” (P. 138)

Here the acts of the railroad through its employees, especially the conductor, in continuing to operate constitutes a waiver.

Finally this court considered waiver in a contract to which a railroad was a party: *Stannick v. Jones*, 252 Fed. 345, *modified* 256 Fed. 354, *motion denied* 258 Fed. 990, *cert. denied* 250 U.S. 664, 40 S. Ct. 11, 63 L. Ed. 1196. Headnote 6 states:

Where no objection was made to defendant’s delay in furnishing money to construct a railroad, such delay, though a technical breach of the contract, must be deemed waived, and does not deprive defendant of the right to enforce a forfeiture in event of nonperformance by the opposite party.”

### ESTOPPEL BY CUSTOM

We also contend that the Southern Pacific is estopped to assert that the alleged breach caused its loss as a custom of operation had developed between the parties as to how obstructions to clearance which were forbidden by contract were to be disposed of. Industry agreed that no obstructions were to be maintained without written permission. (T. 8) The contract does not cover the frequent contingency of the tracks being obstructed by Industry without Industry’s actual knowl-

edge. For example pieces of lumber were frequently dropped. (T. 102) The parties had developed a way to handle this problem: the railroad employees, especially the depot agent, would notify Booth-Kelly of such obstruction and they would be removed. (T. 99-101) In fact such a procedure was required by the Southern Pacific's Rule 1094 previously set out in part.

It is not unreasonable then to suppose that such was the method of handling track obstructions on spur tracks wherever operated by the Southern Pacific. On a somewhat similar problem the Oregon court in *Green Mt. Log Co. v. C. & N. RRR.*, 146 Or. 461, 471, 30 P. 2d 1047 said:

"It appears that there were 11 shippers of logs over the defendant's railroad at the time mentioned, and the testimony tended to show that the custom of scaling the logs according to the freight scale prevailed and was generally known to the shippers over this railroad.

"A railroad tariff is to be considered much the same as a statute or contract: (Citations) Parol evidence is admissible and every fact is relevant which shows how the usage in particular instances was understood and acted upon by the parties then interested. Particular instances of the parties' previous course of dealing may be shown to establish knowledge of the usage: 17 C.J. 520, 521, section 87."

We do not seek to vary the written contract here. We do rely on a usage which developed between the parties to cover certain contingencies not covered by

the contract; that usage though controlling the relationship of the parties here is not in addition to the contract but relates to a separate matter, how to deal with material which admittedly had no right near the tracks. The contract only created the unimplemented right of the tracks to be free of obstructions.

This usage on which we rely is attested to by "particular instances in the parties' previous course of dealing" and by the railroad's rules themselves. The railroad's rules on this matter probably recognize a widespread custom in dealing with obstructions on spur tracks. Finally it is well established that:

"The practical interpretation of the terms of a contract made by the parties while performing it is universally deemed a safe guide to the intended meaning of the instrument." *Kontz v. B. P. John Furniture Corporation*, 167 Or. 187, 203, 115 P. 2d 319.

## CONCLUSION

In conclusion, it is submitted that the trial court erred with respect to each specification of error presented herein, and that this case should be reversed.

Respectfully submitted,

VEAZIE, POWERS & VEAZIE,  
and JAMES ARTHUR POWERS,



## Appendix I

### APPENDIX

45 U.S.C.A. section 51:

**“Liability of common carriers by railroad, in interstate or foreign commerce, for injuries to employees from negligence; definition of employees**

“Every common carrier by railroad while engaging in commerce between any of the several States \* \* \* shall be liable in damages to any person suffering injury while he is employed by such carrier in such commerce \* \* \* for such injury \* \* \* resulting in whole or in part from the negligence of any of the officers, agents, or employees of such carrier, or by reason of any defect or insufficiency, due to its negligence, in its cars, engines, appliances, machinery, track, roadbed, works, boats, wharves, or other equipment.

“Any employee of a carrier, any part of whose duties as such employee shall be the furtherance of interstate or foreign commerce; or shall, in any way directly or closely and substantially, affect such commerce as above set forth shall, for the purposes of this chapter, be considered as being employed by such carrier in such commerce and shall be considered as entitled to the benefits of this chapter. Apr. 22, 1908, c. 149, section 1, 35 Stat. 65; Aug. 11, 1939, c. 685, section 1, 53 Stat. 1404.”

45 U.S.C.A. section 55:

**“Contract, rule, regulation, or device exempting from liability; set-off**

“Any contract, rule, regulation, or device whatsoever, the purpose or intent of which shall be to enable any common carrier to exempt itself from any

## Appendix II

liability created by this chapter, shall to that extent be void: \* \* \* Apr. 22, 1908, c. 149, section 5, 35 Stat. 66.”

49 U.S.C.A. section 2:

**“Special rates and rebates prohibited.** If any common carrier subject to the provisions of this chapter shall, directly or indirectly, by any special rate, rebate, drawback, or other device, charge demand, collect, or receive from any person or persons a greater or less compensation for any service rendered, or to be rendered, in the transportation of passengers or property or the transmission of intelligence, subject to the provisions of this chapter, than it charges, demands, collects, or receives from any other person or persons for doing for him or them a like and contemporaneous service in the transportation or transmission of a like kind of traffic or message under substantially similar circumstances and conditions, such common carrier shall be deemed guilty of unjust discrimination, which is prohibited and declared to be unlawful. (Feb. 4, 1887, c. 104, section 2, 24 Stat. 379; Feb. 28, 1920, c. 91, section 404, 41 Stat. 479.)”

The above is the text of statute when *China Fire Ins. Co. v. Davis*, 50 F. 2d 389, was decided. Present text is identical except that matter relating to transmission of messages is deleted.

8 O.C.L.A. section 113-108 provides in part:

**“Construction and maintenance of switch connections: Conditions governing: Preference for live-**

### Appendix III

**stock and perishable goods: Proceedings on failure to construct switch: Complaint and investigation: Order: Sharing of expenses.** Any railroad \* \* \* upon application of \* \* \* any shipper tendering intrastate traffic for transportation, shall construct, maintain and operate upon reasonable terms a switch connection with any \* \* \* private side track which may be constructed, where such connection is reasonably practicable and can be put in with safety and will furnish sufficient business to justify the construction and maintenance of the same, and shall furnish cars and transport to the best of its ability any traffic tendered to over or from such \* \* \* private side track, without discrimination in favor of or against such shipper; provided, this shall not be construed to compel a railroad to remove from or deliver on a private side track traffic tendered in less than carload lots; \* \* \* If any railroad shall fail to install and operate any such switch or connection as aforesaid on application therefor in writing by \* \* \* any shipper \* \* \* shipper may make complaint to the railroad commission (public utilities commissioner) of Oregon in the manner provided by sections 113-140, 113-148 and 113-149, and the said railroad commission (public utilities commissioner) of Oregon shall make investigation of the same as provided in the said sections, and shall determine as to the safety, practicability and justification thereof, and shall ascertain the items of reasonable cost of making such connection, and shall make an order as provided in said sections 113-140, 113-148 and 113-149, directing the railroad to comply with the provisions of this section in accordance with such order. Such order shall be enforced as other orders of the said railroad commission (public utilities commissioner) of Oregon fixing a reasonable service are enforced. The railroad shall furnish the rails and fastenings, and the switch, complete with frog and guard rails, and the ties and grading shall be furnished or the expense borne by applicant. (L. 1909,

## Appendix IV

ch. 208, p. 303; L.O.L. section 6901; O.L. section 5847; O.C. 1930, section 61-120.)

8 O.C.L.A. section 113-110:

**“Penalty for violation of section 113-109.** If any company or corporation owning or operating any railroad in this state shall fail or refuse to comply with the provisions of this act, the person injured by such failure or refusal shall be entitled to recover against such railroad company, in any court having jurisdiction, a penalty of \$300 for each week during which such neglect, failure, or refusal shall continue.”





# In the United States Court of Appeals

For the Ninth Circuit

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Appellee,*

and

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Cross-Appellant,*

vs.

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Cross-Appellee.*

---

**Appeal and Cross-Appeal from the United States District Court  
for the District of Oregon.**

**HONORABLE JAMES ALGER FEE, *Judge***

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## **COMBINED BRIEF OF CROSS-APPELLANT AND APPELLEE SOUTHERN PACIFIC COMPANY**

---

KOERNER, YOUNG, SWETT & McCOLLOCH,  
JAMES C. DEZENDORF,  
ALFRED H. CORBETT,

800 Pacific Building, Portland, Oregon,

*Attorneys for Cross-Appellant and Appellee.*

VEAZIE, POWERS & VEAZIE, and  
JAMES ARTHUR POWERS,

611 Corbett Building, Portland, Oregon,

*Attorneys for Cross-Appellee and Appellant.*

**FILED**

**MAR 3 - 1950**

**PAUL P. O'BRIEN,**

**CLERK**



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No. 12340

# In the United States Court of Appeals

For the Ninth Circuit

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Appellee,*

and

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Cross-Appellant,*

vs.

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Cross-Appellee.*

---

**Appeal and Cross-Appeal from the United States District Court  
for the District of Oregon.**

HONORABLE JAMES ALGER FEE, *Judge*

---

**COMBINED BRIEF OF CROSS-APPELLANT  
AND APPELLEE SOUTHERN PACIFIC  
COMPANY**

---

**BRIEF OF CROSS-APPELLANT**

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**JURISDICTIONAL STATEMENT**

This is an action between citizens of different states (Pre-trial Order, T. 33), in which the Cross-appellant seeks the recovery of \$46,568.99 from Cross-appellee.

(Pre-trial Order, T. 37.) Judgment in the sum of \$22,000.00 has been entered, based upon findings of fact and conclusions of law made and entered by the trial court. (Judgment Order, T. 56.) It is contended that the United States District Court for the District of Oregon had jurisdiction of this action on the basis of the above facts, under 28 U.S.C.A., Section 1332 (a) (1); and that the United States Court of Appeals for the Ninth Circuit has jurisdiction of this appeal, under 28 U.S.C.A., Section 1291.

### **STATEMENT OF THE CASE**

(Cross-appellant is referred to herein as "Southern Pacific" or "Railroad" and cross-appellee is referred to as "Booth-Kelly" or "Industry.")

#### **A. Facts Giving Rise to This Action.**

This is an action arising out of an accident to an employee of Southern Pacific which occurred February 8, 1945, on an industrial spur track constructed to serve the plant of Booth-Kelly, across land "used or owned" by Booth-Kelly. (Admitted Facts, T. 34.) While engaged as a brakeman on one of Railroad's trains which was switching over the industrial tracks, the employee Mack D. Powers was injured by being caught between the side of the caboose from which he was detraining and a wood cart which was the property of Booth-Kelly and had been placed and left by Booth-Kelly, its employees or agents alongside said track in such a position that one corner of the cart was 42 inches from the outside

edge of the outside rail of the track. (Admitted Facts, T. 34.)

At the time of the accident there was in effect an industrial track agreement dated June 30, 1941, entered into between Southern Pacific and Booth-Kelly, covering the maintenance and operation of the industrial track facilities serving Booth-Kelly's plant. (Admitted Facts, T. 34.)

Powers brought action against Southern Pacific in the California State court under the Federal Employers' Liability Act. The complaint alleged breach of Southern Pacific's statutory duty of using ordinary care to provide Powers with a reasonably safe place in which to work in that first, Southern Pacific caused and permitted the wood cart to remain on the track and second, it failed to warn him of the presence of the wood cart and the resultant insufficient clearance. At trial the Judge removed the first specification from the jury, instructing as a matter of law that Southern Pacific had no right to remove the cart and in this sense could not be charged with responsibility for permitting the wood cart to be or remain in the position in which it was placed. (Plaintiff's Exhibit 2e, p. 352.) A verdict was returned for Mack Powers.

Shortly after filing the action and before time for answer, Southern Pacific gave notice and made demand and tender of defense upon Booth-Kelly. Defendant denied any liability arising out of the accident and refused to assume defense of the action. Subsequent to the rendering of the judgment against it, and after agree-

ment that settlement should be without prejudice to the contentions of either party, the judgment was compromised by the payment of the sum of \$44,699.46. In addition, Southern Pacific was obligated to pay \$1,869.53 for costs and attorneys' fees in defending the Mack D. Powers' action. (T. 35-6.)

After demand for payment of these sums was refused, Southern Pacific Company filed action against Booth-Kelly in the United States District Court for Oregon.

## **B. Issues Submitted and Decisions of Trial Court.**

The contentions of the parties are set forth in detail in the Pre-trial Order (T. 36-44), which order superseded the pleadings. Similarly the Pre-trial Order set forth the questions of fact and issues of law which were considered determinative of the case. (T. 44-47.)

Southern Pacific contended generally: first, it was entitled as a matter of law to recover under the terms of the spur track agreement the full amount paid in satisfaction of the judgment together with attorneys' fees and costs incurred in defending the Powers action; and, second, that independent of the agreement it was entitled to recover such amount since Booth-Kelly's negligence was the active or primary cause of the injury to Powers.

With regard to recovery under the spur track agreement several questions were presented to the court: first, was Southern Pacific entitled to receive the full amount as damages for breach of the impaired clearance provisions of the contract; second, was Southern Pacific en-



titled to recover under the indemnity provisions of the contract and if so was it entitled to recover the full amount of loss, or was its recovery limited to one-half by reason of the specific language of the indemnity clause relating to concurring negligence.

After entering its Findings of Fact the trial court concluded that Southern Pacific was entitled to recover judgment against defendant for the sum of \$22,000 (T. 55, Conclusions of Law No. 7), which was one-half the amount the court determined to be the damage suffered by Powers (T. 53, Finding of Fact No. 11) and Southern Pacific was not entitled to recover independent of the industrial spur track agreement (T. 55, Conclusion of Law No. 5).

From so much of the judgment of the trial court as disallowed \$24,568.99 of Southern Pacific's claim, it filed this cross-appeal.

## **SPECIFICATION OF ERROR No. 1**

### **BREACH OF CONTRACT**

**The court erred in failing to award damages to cross-appellant in the sum of \$46,568.99 for breach of the impaired clearance provisions of the industrial spur track agreement. (Cross-Appellants Appeal Point No. 2, T. 130.)**

Specifically the court erred as a matter of law in making and entering the following Conclusion of Law in conflict to its previous Findings of Fact:

“Plaintiff is entitled to recover judgment against defendant for the sum of \$22,000 on the contract, together with its costs and disbursements incurred herein.” (Conclusions of Law No. 7, T. 55.)

### Summary of Argument

Since the trial court found that the placing of the wood cart within 42 inches of the track was a breach of the spur track agreement relating to impaired clearances, and found the damage to Powers and liability of Southern Pacific was the natural and necessary result of Booth-Kelly's breach of contract, and further found Southern Pacific suffered loss in the total amount of \$46,568.99, the trial court should have concluded as a matter of law that Southern Pacific was entitled to damages in said amount for breach of the impaired clearance provisions of the industrial spur track agreement.

The trial court made the following Findings of Fact:

“21. The placing and leaving of the wood cart within 42 inches from the track was a breach of the provisions of said agreement relating to impaired clearances.” (T. 54.)

“13. The damage to Powers and the liability of plaintiff was the natural or necessary result of defendant's breach of contract.” (T. 53-4.)

“12. Plaintiff suffered loss in the amount of \$44,699.46 judgment costs and of \$1,869.53 court costs and attorneys' fees, by reason of an act or omission of defendant, its agents or employees to an employee of plaintiff while on the industrial track.” (T. 53.)

**These findings are supported by substantial evidence.**

Section 5 of the industrial track agreement provides in part (T. 8-10):

“Industry agrees that without the written consent of Railroad first had and obtained, no \* \* \* material \* \* \* or obstruction of any character shall be, \* \* \* piled, made, stored or maintained upon or over the premises of Railroad \* \* \*. In the event such written consent is given, Industry agrees to comply with the following minimum clearances:

ITEM	CLEARANCES
Structures, materials, poles or other obstructions of any character, except as shown below;	A minimum side clearance of 6 feet measured horizontally from the outside of nearest track rail
Industry also agrees to comply with all of the provisions of this section with respect to clearances on the property beyond the premises of Railroad * * *.” (T. 8-9.)	

It is an admitted fact that the wood cart was the property of Booth-Kelly and had been placed and left within 42 inches from the track by Booth-Kelly, its agents or employees. (T. 34.) The testimony of witness Nysten developed that the car was being used to store kindling for use in defendant’s crane. (T. 91-2.) It is an admitted fact that the injury to Mack Powers was caused by his body coming in contact with the cart. (T. 34.)

Southern Pacific as a common carrier was not compelled under the Interstate Commerce Act to render service to Booth-Kelly over the industrial spur.

49 U.S.C.A. Section 1 (9).

By contracting to do so for Booth-Kelly’s benefit, it broadened its field of potential liability and subjected itself to possible future burdens of the Federal Employers’

Liability Act. Since Southern Pacific undertook to perform services which it could not by law be compelled to render, it was entitled, in voluntarily undertaking to perform such services, to impose such conditions and limitations as it might desire with respect to liability.

9 Am. Jur., Carriers, Section 737;

*Luton Mining Co. v. Louisville & N. R. Co.*, 276 Ky. 321, 123 SW (2d) 1055.

Booth-Kelley contracted that it would not impair the clearances. By placing the wood cart within 42 inches of the track it impaired the clearances in violation of its agreement. But for the proximity of the cart to the track Powers would not have been injured. Booth-Kelley created the unsafe place to work, thereby causing Southern Pacific to breach its statutory duty to provide Powers with a safe place to work. .

The trial court having found breach of contract and resulting damages, Southern Pacific was entitled to payment in full of the amount of those damages.

25 C.J.S., Damages, Section 24:

“As a general rule \* \* \* the damages to which one party to a contract is entitled because of a breach thereof by the other are such as arise naturally from the breach itself or such as may reasonably be supposed to have been within the contemplation of the parties at the time of making the contract as a probable result of the breach thereof.”

See also *Smith v. Palley*, et al., 130 Or. 282, 289, 279 Pac. 279.

## SPECIFICATION OF ERROR No. 2

### ENFORCEMENT OF INDEMNITY PROVISIONS

The court erred in failing to enter judgment against appellant, for breach of the indemnity provisions of the spur track agreement, in the sum of \$46,568.99, the amount of loss suffered by cross-appellant by reason of an act or omission of appellant, its agent or employees to an employee of cross-appellant while on the industrial spur; or, in the alternative,

The court erred in failing to enter judgment against appellant for breach of the indemnity provisions of the spur track agreement, in the sum of \$23,284.49, one-half the amount of loss suffered by cross-appellant by reason of an act or omission of appellant while on the industrial spur. (Cross-appellant's appeal point No. 1, T. 130-1.)

Specifically the court erred as a matter of law in making and entering the following Conclusion of Law in conflict with its previous Findings of Fact:

“Plaintiff is entitled to recover judgment against defendant for the sum of \$22,000 on the contract, together with its costs and disbursements incurred herein.” (Conclusion of Law No. 7, T. 55.)

The court further erred in making the following Findings of Fact:

“Some elements of negligence on the part of plaintiff concurred to cause the accident.” (Finding No. 14, T. 54.)

“Powers suffered injuries in the amount of \$44,000.00.” (Finding of Fact No. 11, T. 53.)

### Summary of Argument

**POINT ONE:** Since the trial court found that Booth-Kelly was negligent in placing and leaving the cart within 42 inches



of the track and that such negligence was the active, direct, proximate and primary cause of the injury to Powers and since it further found that Southern Pacific suffered loss in the total amount of \$46,568.99 by reason of an act or omission of Booth-Kelly to an employee of Southern Pacific while on the track, the court erred in failing to conclude as a matter of law that Southern Pacific was entitled to be indemnified in the amount of \$44,699.46 judgment costs and \$1,869.53 court costs and attorneys' fees.

**POINT TWO:** It was error for the trial court to reduce the amount of Southern Pacific's recovery because of "some elements of negligence (which) concurred to cause the accident," since those elements of negligence were not specifically charged in the Pre-trial Order.

**POINT THREE:** The language under the second clause of the indemnity provision relating to concurring negligence does not apply where the negligence of Southern Pacific is consequent upon the primary negligence of Booth-Kelly.

**POINT FOUR:** It was error for the trial court to determine Powers' injuries to be \$44,000.00 instead of \$44,699.46, since the payment of the latter amount by Southern Pacific represented the compromise of a jury verdict in a greater sum.

### Point One

The trial court made the following Findings of Fact:

"9. Defendant was negligent in placing and leaving the wood cart within 42 inches from the spur track. (T. 53.)

"10. Defendant's negligence in this regard was the active, direct, proximate and primary cause of the injury to plaintiff's employee Powers. (T. 53.)

"15. Plaintiff was not negligent in the form of the specifications of negligence made by defendant in the Pre-trial Order. (T. 54.)

“12. Plaintiff suffered loss in the amount of \$44,699.46 judgment costs and of \$1,869.53 court costs and attorneys’ fees, by reason of an act or omission of defendant, its agents or employees to an employee of plaintiff while on the industrial track. (T 53.)

“17. Employees of plaintiff observed the position of the cart and operations continued thereafter prior to the accident. (T. 54.)

“18. The loss and damage to Powers were not proximately caused by the conditions mentioned in the previous Findings (Finding).” (T. 54.)

Two sections of the agreement deal with indemnity:

Section 7 which reads in part:

“Industry also agrees to indemnify and hold harmless Railroad for loss, damage, injury or death from any act or omission of Industry, its employees or agents, to the person or property of the parties hereto and their employees, and to the person or property of any other person or corporation, while on or about said track; and if any claim or liability, other than from fire, shall arise from the joint or concurring negligence of both parties hereto, it shall be borne by them equally.”

and Section 18 which reads:

“In addition to but not in qualification of the provisions of Section 7 and 17 hereof, Industry hereby releases and discharges and agrees to indemnify and save harmless Railroad, its agents, successors and assigns, from all liability resulting from the movement of cars and/or operations by Industry upon said track.”

It is established by the Pre-trial Order and by the court’s charge to the jury in the Mack Powers case that

Powers was injured by a wood cart which Booth-Kelly placed and permitted to remain in a position of such close proximity to the track that it struck Powers as he was attempting to leave the caboose. (T. 34, Ex. 2e, p. 355.) It is likewise established by the Powers case that the cart was on the premises of Booth-Kelly (T. 34) and that Southern Pacific had no right to remove the cart and in this sense could not be charged with responsibility for permitting the wood cart to be or remain in the position in which it was placed. (Ex. 2e, p. 351-2.)

Southern Pacific is entitled to full recovery under the indemnity provisions of the contract since the negligence of Booth-Kelly was, as between the parties, the primary and efficient cause of the accident.

Findings of Fact 9 and 10, *supra*;

*Astoria v. Astoria & Columbia River R. Co.*, 67 Or. 538, 136 Pac. 645;

*U.S.F. & G. Co. v. Thomlinson Co.*, 172 Or. 307, 141 P. (2d) 817;

*Southern Pacific Company v. Layman*, 173 Or. 273, 145 P. (2d) 295.

Southern Pacific's only fault, and the only determination made in the case *Powers v. Southern Pacific Company*, was the breach of Southern Pacific's statutory duty of using ordinary care to provide Powers with a reasonably safe place in which to work, in that Southern Pacific failed to warn Powers of the presence of the wood cart and the resultant insufficient clearance. (T. 34-5.) Southern Pacific's only fault toward its employee was

the constructive failure of the duty imposed by statute. It was an error of omission, while Booth-Kelly's affirmative act in placing the cart and leaving it in position caused the accident.

In argument during trial, counsel for Booth-Kelly stressed the fact that Southern Pacific had been found negligent with regard to its employee Powers. He argued from this fact that Southern Pacific is barred from asserting the indemnity provision of the contract. Carried to its logical conclusion this theory would preclude any indemnitee from recovering under an indemnity agreement.

Oregon decisions, in keeping with those in other jurisdictions, reveal that indemnity contracts are usually, in the absence of special language, interpreted to be intended to provide against loss or liability of one party through the act of the other, or caused by physical conditions that are under the control of the other, and over which the party indemnified has no control. As previously stated, the spur track here ran over land "owned or used" by Booth-Kelly and it was determined that Southern Pacific had no right to remove the cart. It was, thus, under the control of Booth-Kelly.

In considering and applying the findings of the trial court, it is important to recognize that the question presented to the trial court was the responsibility *as between Booth-Kelly and Southern Pacific under the industrial track agreement*. We specifically call this court's attention to the Oregon case *Astoria v. Astoria & Columbia River R. Co.*, 67 Or. 538, 136 Pac. 645, which is similar



on the facts and is direct authority for Southern Pacific's claim for full recovery under the spur track agreement.

The *Astoria* case involved an action brought by the City to recover over from defendant railroad company the amount of a judgment recovered by Annie Anderson for personal injuries. She had fallen from an elevated railroad leading from the railroad crossing, at which point no barrier had been placed. The railroad had been granted a 50-foot right of way under a City ordinance which provided that the railroad was under a duty to lay its track even with the grade of the elevated street and keep the street crossing in good condition and repair. Although defense was tendered to the railroad, it denied liability. After judgment against the City, action was brought against the railroad for the amount of the judgment plus attorneys' fees and costs of defending the Anderson action. Judgment for the plaintiff City was affirmed.

Four controversial points were decided on the appeal:

1. The City and the railroad did not stand *in pari delicto* with respect to the injury suffered by Miss Anderson, and the fact that the parties stood in *in delicto* each to the other did not foreclose contribution. The court said:

"From a resume of the salient features of the declaration, it plainly appears that the active negligence charged is against the railroad company, while passive negligence only is laid at the feet of the municipality. All that is urged against the city is its failure properly to care for the safety of the traveling public, by not providing barriers along the



street where the accident occurred. While the city failed to perform its full duty in not requiring the company to construct and maintain aprons sufficient to protect the public from harm, and in not seeing that proper barriers were placed along the track where injury was possible, and, for that account, was liable to Annie Anderson, yet that situation does not render the parties equally delinquent. The efficient and primary cause of the accident was the negligence of the company, while the subsequent negligence of the city in not enforcing obedience to the terms of the ordinance was constructive rather than actual."

2. The judgment in the case brought by Annie Anderson was conclusive of the facts which were there the subject of controversy, since the railroad was notified of the pendency of the action. The scope of estoppel in that case embraced all issues determined by it.

3. Costs and attorneys' fees constituted appropriate items of damage for which the City might claim indemnity.

4. The railroad was given such notice of the pendency of the Anderson action as rendered the judgment recovered therein conclusive against the railroad.

Commenting on this case, the Oregon court said in a later decision:

"The defective condition was caused by the railroad company in laying its tracks at a grade above street level in violation of the terms of its franchise. The City was held liable by reason of its failure to enforce an ordinance requiring the company to repair the defect. In this case the parties were not *in pari delicto*. The railroad company was primarily negligent while the negligence of the city was secondary.

The railroad company was bound to indemnify the city by virtue of its contractual relationship. It was not a question of contribution between joint tortfeasors whose active and concurrent negligence caused the injury."

*Fidelity and Casualty Co. of N.Y. v. Chapman*,  
167 Or. 661, 120 P. (2d) 223.

In *Southern Pacific Company v. Layman*, 173 Or. 273, 145 P. (2d) 295, which stands for the proposition that an indemnity provision will not be interpreted to indemnify the indemnitee against loss suffered *solely* by reason of his own negligence, in the absence of such intention expressed in unequivocal terms, the Oregon court indicated that under a factual situation similar to that presented in the instant case, the indemnity provision would be invoked in favor of Southern Pacific. The court said:

"By the terms of the contract now in question it was the duty of the defendant to maintain and keep the crossing in good repair, and it is readily conceivable that his negligent failure to discharge that obligation might be the primary cause of an accident to one of the defendant's trains, which would result in injury to passengers and a consequent liability to the defendant. In such a case the plaintiff would evoke the indemnity clause of the contract. An interpretation which limits the general language of the agreement to instances of that character suffices to give effect to the agreement and, in our opinion, is reasonable."

### Point Two

Although the trial court found that Southern Pacific was not negligent in the form of the specifications of

negligence made by defendant in the Pre-trial Order (Finding of Fact No. 15, T. 54), the court in its 14th Finding stated, "Some elements of negligence on the part of plaintiff concurred to cause the accident." (T. 54.)

Evidently based on this latter finding, and the language in Section 7 of the spur track agreement relating to concurring negligence, the trial court entered judgment for \$22,000 instead of for the full amount required to compromise the judgment and pay court costs and attorneys' fees.

There was no basis for the trial court's Finding of Fact No. 14, either in proof, pleadings or issues framed by the Pre-trial Order.

Federal Rules of Civil Procedure, Rules 8, 15.

The Pre-trial Order provides that it superseded the pleadings. (T. 49.) It was error for the trial court to make a finding of concurrent negligence, on grounds not made an issue in the pleadings, and which Southern Pacific had had no opportunity to meet with testimony or by argument.

*Fehely v. Senders*, 170 Or. 457, 135 P. (2d) 283.

### Point Three

Assuming without admitting that Southern Pacific was guilty of some negligence which concurred to cause the accident, the language under the second clause of the indemnity provision in Section 7, relating to concurring negligence does not apply where the negligence of

Southern Pacific is consequent upon the primary negligence of Booth-Kelly.

*Astoria v. Astoria & Columbia River R. Co.*, 67 Or. 538, 136 Pac. 643;

*Deep Vein Coal Co. v. Chicago & E. I. R. Co.*, 71 Fed. (2d) 963.

The decision in the *Astoria* case supporting this statement has already been cited and quoted at length. In the *Deep Vein* case, defendant's mines were served by a switch track which the railroad had constructed under a written contract whereby the coal company agreed to indemnify and save the railroad harmless for:

"loss, damage or injury from any act or omission of the coal company, its employees or agents, to the person or property of the parties hereto and their employees and to the person or property of any other person or corporation while on or about said tracks, and if any claim or liability, other than from fire, shall arise from the joint or concurring negligence of the parties hereto, it shall be borne by them equally."

The contract also contained a provision that the coal company would not erect or allow to be erected any building, structure, fixture or any pile of any kind in dangerous proximity to the track, and the coal company would indemnify and save harmless the railroad against loss, damage or expense in consequence of injury to or death of any person by reason of or growing out of the location of any such building, structure, fixture or pile.

An accident happened by reason of the maintenance by coal company of a line of poles. By agreement, the

railroad settled with the injured man. Contending that the first quoted paragraph applied, the coal company paid one-half the amount of settlement, but refused to pay the other half. In granting full recovery to the railroad the court said:

“It seems to us that the joint or concurring negligence covered by paragraph 8 is not the negligence of one party consequent upon the primary negligence of the other. But be that as it may, paragraph 10 definitely and specifically covers such a case as this.”

In the case at bar the negligence, if any, of Southern Pacific was consequent upon the primary negligence of Booth-Kelly in placing and leaving the cart within 42 inches of the track, in violation of the specific provisions of the spur track agreement.

Instances where an injury was the result of the concurring negligence of the two parties may be conceived, as where the railroad and an employee of Industry pushing a cart or driving a vehicle were concurrently approaching a given point on the track. But those are not the facts in the instant case.

Under the law as enunciated in the *Astoria* and *Deep Vein* cases Southern Pacific is entitled to recover the full amount of its loss, and entry of judgment in any lesser amount is error.

#### **Point Four**

The payment by Southern Pacific of the sum of \$44,699.46 was in compromise of a jury verdict and judg-



ment in the sum of \$46,110.00. (Plaintiff's Exhibits 2f and 2g.) The trial court erred in independently determining Powers' damage to be \$44,000.00, since this question was litigated and decided in the action Powers v. Southern Pacific Company and thus was binding on the parties to the instant action. (Admitted Facts, T. 36.) The judgment of the trial court should therefore have included the sum of \$44,699.46 as well as attorneys' fees and costs.

### **SPECIFICATION OF ERROR No. 3**

#### **RECOVERY INDEPENDENT OF CONTRACT**

The court erred in failing to award recovery to cross-appellant in the sum of \$46,568.99 independent of contract, because appellant's negligence in placing and leaving the wood cart within 42 inches from the spur track was the active, direct, proximate and primary cause of the injury to cross-appellant's employee Powers, and of cross-appellant's resulting liability. (Cross-appellant's appeal point No. 3, T. 131.)

Specifically the court erred as a matter of law in concluding, in conflict with its Findings of Fact, as follows:

"Defendant is not obligated to pay plaintiff \$44,568.99 (\$46,568.99) or any part thereof, independent of the industrial spur track agreement."

(Conclusion of Law No. 5, T. 55.)

#### **Summary of Argument**

Since the trial court found Booth-Kelly was negligent in placing and leaving the wood cart within 42 inches from the spur track and its negligence in this regard was the active, direct, proximate and primary cause of the injury to Powers

and since it further found Southern Pacific was not negligent in the form of the specifications of negligence made by Booth-Kelly in the Pre-trial Order, the trial court should have concluded as a matter of law that Southern Pacific was entitled to recover from Booth-Kelly the full amount of loss suffered by it.

*Shearman & Redfield Negl.*, Rev. Ed., §894.

*Scott v. Curtis*, 195 N.Y. 424;

*Lowell v. Boston & Lowell R. Corp.*, 23 Pick 24;

*Astoria v. Astoria & Columbia River R. Co.*, *supra*.

Independent of indemnity provisions in agreements covering the performance of work, and in some instances wholly apart from any contractual relationship, the rule of law is laid down that recovery will be allowed against the active wrongdoers.

“One liable only by reason of a duty imposed by law for consequences flowing from the negligent conduct of another, and not an actual participant in that conduct, may recover over against the active perpetrator of the wrong. The latter stands in the relation of an indemnitor to the former.”

*Shearm. & Redf. Negl.*, Rev. Ed., Sec. 894.

In *Scott v. Curtis*, 195 N.Y. 424, action was brought by Scott for the amount of damages paid by him to a third person who fell into the coal chute serving Scott's property, allegedly because of the negligent manner in which defendant's employees had covered the chute. A verdict for Scott was reversed without prejudice since no evidence had been introduced showing how the accident had occurred. The court stated: “It may be assumed this action will lie” if the accident occurred by reason of

the negligent manner in which defendant's employees temporarily covered or guarded the hole.

By way of guidance at the new trial, the court had this to say concerning the relationship of the parties between themselves:

"The liability of the owner of real property for injury to a passer-by for negligence in covering or in failing to cover or guard such a hole in a sidewalk does not relieve the active or actual wrongdoers from the consequences of their acts. The liability to the passer-by is joint. As between themselves the active wrongdoer stands in the relation of an indemnitor to the person who has been held legally liable therefor."

In the case *Lowell v. Boston & Lowell Railroad Corp.*, 23 Pick. 24, where, unlike the *Astoria* case, there was no contract or franchise, the railroad made a cut in the street in the course of building a new line. Barriers at the cut were left down and a third person was injured. The town, on being held liable, brought this action against the railroad. A judgment for the town was affirmed. The court discussed the general rule concerning joint tort-feasors, then said:

"Our law, however, does not in every case disallow an action by one wrongdoer against another, to recover damages incurred in consequence of their joint offense. The rule is *in pari delicto potior est conditio defendentis*. If the parties are not equally criminal, the principal delinquent may be held responsible to his co-delinquent for damages incurred by their joint offense. \* \* \* But when the offense is merely *malum prohibitum*, and is in no respect

immoral, it is not against the policy of the law to inquire into the relative delinquency of the parties, and to administer justice between them, although both parties are wrongdoers.”

This rule is also set out in the *Astoria* case, previously discussed in this brief under Specification of Error No. 2.

The rules of law set forth in these authorities are applicable here because plaintiff did not participate in the original wrong—in the placing of the cart. Hence recovery in the full amount should be awarded Southern Pacific, independent of contract.

**BRIEF OF APPELLEE**  
**SOUTHERN PACIFIC COMPANY**

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**ANSWER TO BOOTH-KELLY'S STATEMENT  
OF THE CASE**

(Appellant is referred to herein as "Booth-Kelly" or "Industry" and Appellee is referred to as "Southern Pacific" or "Railroad")

Counsel for Booth-Kelly has combined argument with fact in his Statement of the Case, sometimes without express designation. Besides this failure of designation, counsel has also failed to carry the argument over into the portions of his brief devoted to Specifications of Error. By this organization of his brief, counsel has created a problem in the orderly refuting of Booth-Kelly's points, and we therefore make these comments, lest the court accept counsel's Statement of the Case at face value.

An example is the assumption that the service performed by Southern Pacific at the time of the accident did not either directly or indirectly benefit Booth-Kelly. We view this contention as immaterial to the case, since consideration for the contract as a whole was amply established, but wish to point out there was no determination on this point either in the Powers case or by the trial court. Even should the point be considered worthy of the court's attention, the facts are as consistent with a finding of benefit to Booth-Kelly as with a finding of sole benefit to the Railroad.



Again on page 5 of the Statement counsel argues that the spur track agreement, upon which this action is partially based, was Southern Pacific's unilateral redraft of old agreements. Again there was no finding to this effect by the trial court. Not only is this contention immaterial, but it is incorrect. The previous agreements were admitted in evidence subject to Southern Pacific's objections, but if the subject is thought germane by this court, then a comparison of the older agreements with the 1941 spur track agreement would show that Booth-Kelly was given certain privileges in connection with the maintenance of unloading facilities, and the use of the crane set-out spur, which had not previously existed.

Again counsel misinterprets the Oregon statute, without even stating his interpretation is subject to question, in connection with the extent of a common carrier's duty to furnish service over a private side track. This point is argued under Booth-Kelly's Specification of Error III and will be answered later in this brief.

## **ANSWER TO BOOTH-KELLY'S SPECIFICATION OF ERROR NO. I**

### **Summary of Argument**

The trial court correctly concluded that the determinations in the Mack Powers action against Southern Pacific are not *res adjudicata* in this action, because the question of ultimate responsibility as between Booth-Kelly and Southern Pacific for the damage and loss suffered by Powers was not litigated in that action.

The fundamental question involved in the instant case is the responsibility as between Booth-Kelly and Southern Pacific for the damage to Powers and the loss thereby occasioned to Southern Pacific. In resolving that question, the primary responsibility of Booth-Kelly for the accident and its obligations under the contract are important.

The trial court not only found that Booth-Kelly breached the impaired clearance provisions of the spur track agreement, but also was negligent in placing and leaving the cart in position and that such negligence was the primary cause of the injury to Powers. Counsel has advanced no evidence which would justify setting aside these findings (see Federal Rules of Civil Procedure Rule 52(a)) but argues the decision in the Powers case prevents any such findings being made.

The Powers case was concerned only with a determination of Southern Pacific's responsibility to its employee under the Federal Employers Liability Act, and with the amount of damage suffered by Powers. No question of relative responsibility as between Southern Pacific and Booth-Kelly was there determined. No spur track agreement was discussed or applied, and indeed would have been immaterial in the trial of Powers' claim against the Southern Pacific.

We agree that just as Booth-Kelly must abide by the determinations actually made in the Powers case, so must Southern Pacific in seeking recovery from Booth-Kelly accept the findings in the Powers case upon questions there litigated and determined. The findings in

the Powers case, however, are not inconsistent with the findings entered by the Court in the instant case.

Since the trial court determined that Booth-Kelly's negligence was the primary cause of the accident, and in the light of the spur track agreement, Southern Pacific is entitled to recover in full from Booth-Kelly.

*Astoria v. Astoria & Columbia R. R. Co.*, 67 Ore. 538, 136 Pac. 645;

*Hudson Valley Railway Co. v. Mechanicville E. L. & G. Co.*, 180 App. Div. 86, 167 N.Y.S. 428.

In the *Hudson Valley* case, cited by counsel in his argument under Point One, defendant Electric Company allowed its power line to sag on top of electric railway's wire, causing the wire to burn in two, drop to the street and kill a horse. The owner sued and recovered judgment against both Electric Company and the Railway, and collected from the latter. Railway sued the Electric Company, alleging the latter was primarily liable, and obtained a jury verdict and judgment. Based upon the previous decision holding the parties jointly liable, the trial court set the judgment aside. Held error.

The Appellate Court stated the previous judgment merely showed both parties were liable to the owner. The general rule against contribution did not apply where the Electric Company did the act or created the condition and the Railway Company did not actively join in—although the latter might have taken precautions to protect the public.

The *Astoria* case, on its facts, is analogous to the instant case. There, the City brought action to recover over from Railroad Company the amount of a judgment recovered by Annie Anderson for personal injuries. She had fallen from an elevated roadway leading to the railroad crossing, at which point no barrier had been placed. Railroad had been granted a 50 foot right-of-way under a City ordinance which provided the Railroad was under a duty to lay its track even with the grade of the elevated street and keep the street crossing in good condition and repair. Defense was tendered to the railroad and refused.

In granting recovery to the City against the Railroad, the Court determined after full discussion that the parties were not *in pari delicto*. After examining the complaint filed by Miss Anderson in the action against the City, the Court stated:

“From a resume of the salient features of the declaration, it plainly appears that the active negligence charged is against the Railroad Company, while passive negligence only is laid at the feet of the municipality. All that is urged against the City is its failure properly to care for the safety of the traveling public, by not providing barriers along the street where the accident occurred. While the City failed to perform its full duty in not requiring the Company to construct and maintain aprons sufficient to protect the public from harm, and in not seeing that proper barriers were placed along the track where injury was possible, and, for that account, was liable to Annie Anderson, yet that situation does not render the parties equally delinquent. The efficient and primary cause of the accident was the negligence of the Company, while the subse-



quent negligence of the City in not enforcing obedience to the terms of the ordinance was constructive rather than actual."

In commenting on this case, the Oregon court said in a subsequent decision, *Fidelity & Casualty Co. of N.Y. v. Chapman*, 167 Ore. 661, 120 P. (2d) 223:

"In this case the parties were not *in pari delicto*. The Railroad Company was primarily negligent while the negligence of the City was secondary. The Railroad Company was bound to indemnify the City by virtue of its contractual relationship. It was not a question of contribution between joint tort feasers whose active and concurrent negligence caused the injury."

None of the authorities cited by counsel under his argument under Point One go further than holding an indemnitee cannot, in a later action against indemnitor, deny facts litigated and determined in the case upon which the demand for indemnity is based.

In the case *Edinger & Co. v. S. W. Surety Ins. Co.*, 182 Ky. 340, 206 S. W. 465, recovery against Edinger & Co. depended upon proof of a vicious animal, which put the damage within an exception clause in the insurance policy. In the *Central of Georgia Railway Co. v. Macon Ry. & Light Co.*, 9 Ga. App. 628, 71 S. E. 1076, no contract was involved.

The *Hudson Valley* case supports Southern Pacific's position.

As we read the comments under Section 1067, *Restatement of Laws, Judgments*, the quotation cited was



not meant to apply to a situation where a contract exists, or where the primary negligence of the indemnitor caused the accident. We also wish to point out that under *Comment i*, the right of indemnitee to recover the amount of expenses for attorney's fees in defending the previous action, is supported.

Counsel cites no evidence justifying reversal of Finding No. 18, hence it should not be disturbed. *Fed. Rules of Civ. Proc.*, Rule 52 (a). The reference to previous "Findings" is, we believe, a typographical error, and Finding No. 17 only, relating to knowledge of position of the cart, was referred to in Finding No. 18.

Although some of the cases cited by counsel under his argument in Point Two are far afield from the situation here involved, we agree, as we previously stated, that so far as indemnitee is concerned the scope of estoppel created by the judgment in the primary case embraces all of the issues determined by it. *Astoria v. Astoria & Columbia R. R. Co.*, 67 Ore. 538, 136 Pac. 645, *supra*.

## ANSWER TO BOOTH-KELLY'S SPECIFICATION OF ERROR NO. II

### Summary of Argument

The determinations in the Powers case established only that Southern Pacific failed to provide its employee with a safe place in which to work in that it failed to warn him of the presence of the wood-cart, and that Powers suffered injuries in the amount of at least \$44,699.46. Booth-Kelly was respon-

sible for Southern Pacific's failure to provide a safe place to work.

Since those determinations did not concern the question of responsibility as between the parties to this proceeding, the trial court properly found that Booth-Kelly's negligence in placing and leaving the cart within 42 inches from the track was the active, direct, proximate and primary cause of the injury to Powers.

In order to determine what was decided in the Powers case it is necessary to examine the proceedings upon which judgment was there obtained. It was agreed in the Pre-trial Order and found by the trial court that:

"The complaint alleged breach of Southern Pacific Company's statutory duty of using ordinary care to provide said Mack D. Powers with a reasonably safe place in which to work in that \* \* \* it failed to warn him of the presence of the wood-cart and the resultant insufficient clearance." (Admitted Facts, T. 34-5; Findings of Fact, T. 52.)

Thus upon judgment for Powers it was determined that Southern Pacific had breached its statutory duty of providing its employee with a safe place within which to work.

The primary cause of that breach was the placing and leaving of the wood-cart by Booth-Kelly. This was not only a negligent act primarily causing the injury, it was in specific violation of Booth-Kelly's obligations under the impaired clearance provisions of the contract.

The question of ultimate responsibility as between Booth-Kelly and Southern Pacific for the accident was not litigated or determined in the Powers case. Counsel

argues the Powers case determined that the accident resulted from the sole negligence of Southern Pacific. No such determination was made. The action established a breach of Southern Pacific's duty under the Federal Employers' Liability Act. Furthermore, had Powers been unable to collect from Southern Pacific, he could have sued Booth-Kelly and under the facts, could have recovered.

The Powers case did establish Booth-Kelly's responsibility for the presence of the cart. It is an admitted fact and was found by the court that the wood-cart was the property of Booth-Kelly and had been placed and left by it or its employees alongside the track on premises owned or used by Booth-Kelly. (T. 34, T. 52.)

In view of these facts, and since the findings of the trial court with respect to Booth-Kelly's negligence in placing and leaving the cart are not in conflict with matters litigated in the Powers case, no error was committed in entering Findings of Fact 9 and 10. *Fed. Rules of Civ. Proc.*, Rule 52 (a).

There is no finding by the trial court that failure to warn was an independent act of negligence and counsel's argument in this connection is therefore out of place in this appeal. As pointed out, the Powers case established the breach of a statutory duty. It is the question of ultimate responsibility for that breach that is important in this case.

Counsel's authorities under the heading "Failure to Warn" are not in point. *City of Seattle v. Peterson & Co.*, 99 Wash. 533, 170 Pac. 140, turns on a finding by the

jury in a previous case that the City had failed to maintain proper equipment to ground its electrical system, while the contractor's bond was limited to negligence of the contractor in the performance of his work. *City of Puyallup v. Vergowe*, 95 Wash. 320, 163 Pac. 779, was determined by reason of a finding of negligence against the City in failing to have street lights operating, which was again a matter separate from the contractor's duty.

In the instant case, Southern Pacific's breach of its statutory duty was caused by Booth-Kelly's negligent act by placing the wood-cart and the negligent omission to remove it, in direct violation of the impaired clearance provisions of the contract.

The quotation from *U.S.F. & G. Co. v. Thomlinson Co.*, 172 Ore. 307, 141 Pac. 817, is not in point, since it deals with sole negligence. Later in its opinion the court stated:

"Where, however, two have been held liable to a third person for negligence, but as between themselves one of them is entitled to indemnity from the other an entirely different situation arises. \* \* \* It is clear that the fact of the judgment in the Malben case and of the settlement in the Redd case established that both defendants therein owed money to the injured parties, but the judgment did not, as between themselves, determine which of the defendants was negligent or whether either of them was entitled to indemnity from the other."

Counsel's argument under Point Two likewise fails, since the Powers case determined only that Southern Pacific breached its statutory duty. Counsel lays great stress on cases from outside jurisdictions, and makes no



effort to apply Oregon decisions such as the *Astoria* case to the issues on this proceeding. *Wm. Cameron & Co. v. Thompson*, . . . Tex. Civ. App. . . ., 175 S. W. (2d) 307, is distinguishable because of the element of control over the object causing the injury, and because no breach of contract is involved. In the *Thompson* case, railroad company's crew negligently blocked the hand truck and failed to close the car door after being in the car. It had control over the hand truck and the car.

In the instant case, on the other hand, placing and leaving the cart was a breach of contract and Southern Pacific had no right to remove the cart. It was not, according to the instructions of the trial judge in the Powers case, negligent in allowing the cart to remain in position and had no right to remove it. (Reporter's transcript, *Powers v. S. P. Co.*, p. 355-6.)

No agreement was involved in *Central & Georgia Ry. Co. v. Swift & Co.*, 23 Ga. App. 346, 98 S. E. 256, a case in which no opinion was written. *Glappa v. Detroit Etc. R. Co.*, 179 Mich. 76, 146 N.W. 134, involved an appeal by railroad from an adverse judgment recovered by a teamster. The question of Railroad's liability to the teamster was solely involved.

## ANSWER TO BOOTH-KELLY'S SPECIFICATION OF ERROR NO. III

### Summary of Argument

The trial court correctly found there was consideration for the spur track agreement as a whole, since Southern Pacific was not obligated by law to furnish service on the spur track.



Since there was consideration for the agreement involved in this action, it is immaterial whether or not the indemnity provision existed in prior agreements.

1. *A recovery in the California case by Powers under the Federal Employers' Liability Act established that interstate commerce was involved at the time of the accident. Hence provisions of the Interstate Commerce Act would apply.*

Section 51 of Title 45 U.S.C.A. under which recovery was sought by Powers, provides in part:

“Every common carrier by railroad while engaging in commerce between any of the several states \* \* \* shall be liable in damages to any person suffering injuries while he is employed by such carrier in such commerce \* \* \*.”

Although the Federal Employers' Liability Act affords considerable latitude to employees in the proof of interstate operations, the application of that act to the Powers claim constituted a determination that interstate commerce was involved at the time of the accident. No contention was made and no evidence was furnished by Booth-Kelly to the contrary in the trial court. Therefore the requirements of the Federal law, with regard to railroad operations over private industrial spur tracks, are applicable.

2. *Under provisions of the Interstate Commerce Act Southern Pacific was not obligated to undertake operations over the Booth-Kelly spur track.*

Section 1 (9) of Title 49 U.S.C.A. provides in part:

“Sec. 1 (9) Switch connections and tracks. Any common carriers subject to the provisions of this chapter, upon application of any \* \* \* shipper tendering interstate traffic for transportation, shall construct, maintain and operate upon reasonable terms a *switch connection* with any such \* \* \* private side track which may be constructed to connect with its railroad, where such *connection* is reasonably applicable and can be put in with safety and will furnish sufficient business to justify the construction and maintenance of the same; and shall furnish cars for the movement of such traffic to the best of its ability without discrimination in favor of or against any such shipper.” (Emphasis supplied.)

If Booth-Kelly's interpretation of the law is correct, no contract would have been required. However, it is established that a railroad is not obligated to give service over a private industrial spur track and that an agreement to operate over such track is sufficient consideration for indemnity provision in a contract covering operations over the spur track.

The question of consideration was discussed in detail in *Luton Mining Co. v. Louisville & N. R. Co.*, 276 Ky. 321, 123 S.W. (2d) 1055, an action brought by the railroad against the mining company to recover the sum of money paid in comprising a claim for death of a brakeman, killed when his foot was caught in an unblocked frog while trying to loosen the brakes of a car. The brakeman at the time of the injury was using a pole while standing on the ground, in violation of company rules.

In 1918 the company made a contract with the railroad for the construction of a switchyard and connection. This contract, according to the decision, contained a provision that the mining company would hold harmless the director general and railroad company from all claims and demands arising directly or indirectly out of the maintenance of said tracks or the operation of rolling stock thereon.

It was claimed by the mining company that the contract was without consideration, was without mutuality, that it was discriminatory and was obtained by coercion.

The court found no evidence of coercion, and refuted the argument of the mining company that the railroad was required under law to furnish the switch connection, whereas to get the connection the mining company had to assent to the indemnity provisions. The court stated it was frequently held that contracts of this type are valid and in no sense contrary to public policy, citing *Gorman Coal Co. v. Louisville & N. R. Co.*, 213 Ky. 551, 281 S.W. 487; *New Orleans Great Northern Railway Co. v. St. Aleus & Co.*, 159 La. 36, 105 S. 91; *John Griffith's & Son v. National Fireproofing Co.*, 310 Ill. 331, 141 N.E. 739.

The *Luton* opinion goes on to discuss the matter of mutuality and consideration. The court states that the mining company's argument overlooks the fact that by the contract the railroad also bound itself to do things not required by law, i.e.:

(a) to construct the track, and under the *Gorman* case this was sufficient consideration, and (b) to undertake to place empty cars on the switch track and take loaded cars therefrom. The court then goes on to state:

“It is not required by law to perform this service. The only obligations imposed on it were by virtue of paragraph 9 of Section 1 of the Interstate Commerce Act, as amended, 49 U.S.C.A., Sec 1 (9), which provides:

(quoting the statute above set out)

“It is apparent from a reading of this section of the statute that *no duty is imposed upon the railroad company beyond its own right of way. Except for the contract, the mining company would have had the duty and burden of moving empty and loaded cars to and from the switch covered by the contract.* The rule announced in *Cleveland C. C. & St. L. R. R. v. U. S.*, 275 U. S. 404, 48 Sup. Ct. 189, 72 L. Ed. 338, is not in conflict \* \* \*. (it) decided only that the railroad company \* \* \* could be compelled to make the *switch connection* when demanded by the shipper. We are of the opinion, therefore, that there was mutuality of contract and that no coercion or discrimination is proven or can be deduced from the contract itself.” (Emphasis supplied.)

In this case, since Southern Pacific undertook to perform services which it could not be compelled to render, it could, in voluntarily undertaking to perform such services, impose such conditions and limitations as it might desire with respect to liability.

9 *Am. Jur., Carriers*, Sec. 737.



3. *Even should Oregon law apply, its provisions, like those of the Federal law, do not require operations over an industrial spur track.*

As can be seen by the wording of Sec. 113-108 O.C.L.A. set out in full on Page II of the appendix of Booth-Kelly's brief, the Oregon statute relating to construction and maintenance of switch connections uses substantially the same language as the provisions of the Interstate Commerce Act. Here again the railroad's obligation in connection with construction stops with building a switch connection, and its obligation with regard to operations ceases with its delivering cars to the switch connection. In this regard the Oregon law is identical with Federal law.

As under Federal law, application for the enforcement of this section can be made to the Public Utilities Commissioner. If counsel's interpretation of the law were correct it is inconceivable that Booth-Kelly and other industries similarly situated would not have requested such relief.

Counsel also cites Sec. 113-104 requiring railroad to keep and maintain adequate and suitable "switches, spurs, and side tracks for receiving, handling and delivering freight \* \* \*." By general interpretation this section is limited to the construction of switches and spurs and side tracks on a railroad's own premises available for use by all shippers.

*Southern Pac. Co. v. Railroad Comm.*, 60 Ore. 400,  
119 Pac. 727.



We can see no purpose except obfuscation in citing Section 113-109 O.C.L.A. Booth-Kelly has never contended it operated a warehouse, the accident happened more than 150 feet from the main line of the railroad, and there is no evidence in the record that a public warehouse was involved in this case.

Subsections (18) to (22) inclusive of Section 1, 49 U.S.C.A. concern the question of necessity for Interstate Commerce Commission orders relating to construction or abandonment of industrial and spur tracks, and not with the duty of a railroad to agree to serve an industry over a private track.

4. *Whether or not the indemnity provision was inserted in a revised contract is immaterial.*

Inasmuch as Southern Pacific was not obligated to agree to give Booth-Kelly service over the private spur track, it could impose such conditions as it might desire, before contracting to assume this service. While we contend the court should confine its decision to the 1941 agreement, and objected to the introduction of the previous agreements we wish to point out that other concessions were granted in the 1941 agreement, such as the use and maintenance by Booth-Kelly of the crane set-out spur and reload facilities. The indemnity provision of the contract was part of the bargained for consideration, and Booth-Kelly should not at this late date attempt to eliminate part of the contract.

## ANSWER TO BOOTH-KELLY'S SPECIFICATION OF ERROR NO. IV

### Summary of Argument

The indemnity provisions of the contract apply without regard as to whether or not Southern Pacific was directly serving Booth-Kelly since the obligation is clearly expressed and there is consideration for the contract as a whole, however the question is immaterial since no Finding of Fact was made by the trial court as to benefit to Booth-Kelly and the question was not included in Booth-Kelly's Specifications of Error.

Section 7 of the agreement contains two separate contractual provisions, stated in separate paragraphs. The first paragraph consists of an "exemption" contract and relates solely to fire damage. It relieves Southern Pacific from actions by Booth-Kelly or others for fire damage to the property of Booth-Kelly, or other property on Booth-Kelly's premises, arising out of Southern Pacific's operations while serving Booth-Kelly. These exemption provisions have long been used by railroads and their validity and the rights of the contracting parties thereunder have long been established.

The second sub-paragraph contains provisions indemnifying Southern Pacific in the event of damage to its employees or property from an "act or omission" of Booth-Kelly. These provisions concern an entirely separate matter, and are governed by separate case law.

Counsel claims under four rules of construction that the words "serving industry" can be carried over from

the exemption contract to the indemnity provision. These will be answered in order.

1. A consideration of the entire instrument shows that the matter of Southern Pacific's liability for fire was separately treated from the matter of Booth-Kelly's liability for its acts or omissions.

The contract contains a variety of separately stated situations where the rights, duties and obligations of the parties are carefully defined. The first sub-paragraph deals with damage arising out of fire, and separately expresses a limitation upon the liability of Southern Pacific. The second paragraph separately states the extent of liability assumed by Booth-Kelly.

2. The first and second paragraphs are not repugnant or incompatible, let alone inconsistent.

There is no incompatibility in the wording of the two paragraphs. The meaning is clear. Southern Pacific is liable for fire damages only when *not* serving industry. Booth-Kelly is liable for its act or omission causing injury whether or not Southern Pacific is using the track to serve it. The two clauses deal with different situations and far from being repugnant or even inconsistent, are merely inconvenient to the validity of Counsel's argument.

3. The rules of construction against the preparer does not apply where the meaning is clear.

Counsel's argument, especially in the light of his remarks under the previous rule of construction, is not so

much that the provisions of the second paragraph are vague, but that they state too clearly an obligation that now is unpalatable to Booth-Kelly. The first paragraph restricts Southern Pacific's relief from liability for fire damages to cases where it is serving Booth-Kelly. The second paragraph contains no such limitation and thus emphasizes to a careful reader, the broad coverage of Booth-Kelly's obligation for damages caused by its act or omission. Counsel is not merely seeking to have the contract construed against the preparer, he is asking that the contract be rewritten.

4. The indemnity provision in Section 7 is valid, and no modification by way of construction is necessary to support its validity.

As proved under our Answer to Specification of Error No. III, there was ample consideration for the contract as a whole, and the contract as a whole does not lack mutuality. See *Luton Mining Co. v. Louisville & N. R. Co.*, 276 Ky. 321, 123 S.W. (2d) 1055. It is well established that consideration is sufficient for as many promises as are bargained for and given in exchange if it would be sufficient for each one of them if that alone were bargained for. *Restatement of Laws, Contracts, Section 83*. Booth-Kelly, having bargained for Southern Pacific's promise to operate over its industry spur, and having given several promises in exchange therefor, should not now be heard in an attempt to split off part of the bargained for consideration.

Counsel has stressed the contention that Southern Pacific was not "serving industry", however the question of whether or not Booth-Kelly was benefitting directly or indirectly from Southern Pacific's operations at the time of the accident was not decided by the trial court, and no Specification of Error was made concerning the point. Therefore the question is immaterial so far as this appeal is concerned.

However, since counsel has "rung the bell", we wish to point out that the spur track agreement covers the entire spur, that the only unloading facilities shown belong to Booth-Kelly, that although Booth-Kelly had virtually ceased to take deliveries over the track since approximately 1939, (witness Nysten, T. 88) the 1941 agreement was executed in its present form. These facts are consistent with direct benefit to Booth-Kelly as landlord or as operator of reload facilities.

## ANSWER TO BOOTH-KELLY'S SPECIFICATION OF ERROR NO. V

### Summary of Argument

Southern Pacific is entitled to full recovery under Oregon as well as general law since Booth-Kelly's act or omission was the primary cause of the accident and Booth-Kelly's primary responsibility for the loss suffered by Southern Pacific was established by contract.

1. *Booth Kelly's act or omission was the primary cause of the damage to Powers.*



The trial court found, in its Findings of Fact:

“9. Defendant was negligent in placing and leaving the wood cart within 42 inches from the spur track.”

“10. Defendant’s negligence in this regard was the active, direct, proximate and primary cause of the injury to plaintiff’s employee Powers.”

In the face of these findings, it is surprising that counsel seeks to build an argument from a passing remark of the court in *Southern Pacific Co. v. Layman*, 173 Or. 273, 145 P. (2d) 295. The *Layman* case arose on demurrer to the answer which asserted that the *sole* cause of the injury was railroad’s negligence. The case stands for the proposition that an indemnity provision will not be interpreted to indemnify the indemnitee against loss suffered *solely* by reason of his own negligence, in the absence of such intention expressed in unequivocal terms.

It is generally recognized that the need for invoking indemnity provisions of a contract does not arise until after the indemnitee has been held responsible in damages to a third person. The true question between indemnitor and indemnitee is responsibility under the terms of the agreement.

In its opinion, the court in the *Layman* case indicates that under a factual situation similar to that presented here, the indemnity provision would be invoked in favor of Southern Pacific. The court said:

“By the terms of the contract now in question it was the duty of the defendant to maintain and

keep the crossing in good repair, and it is readily conceivable that his negligent failure to discharge that obligation might be the primary cause of an accident to one of defendant's trains, which would result in injury to passengers and a consequent liability to the defendant. In such a case the plaintiff would invoke the indemnity clause of the contract. An interpretation which limits the general language of the agreement to instances of that character suffices to give effect to the agreement, and, in our opinion, it is reasonable."

This statement is in keeping with the decision in *Astoria v. Astoria & Columbia R. R. Co.*, 67 Or. 538, 136 Pac. 645, discussed earlier in this brief.

In the case at bar, it was the duty of Booth-Kelly to conduct its operations on or about the vicinity of the track in such manner that the clearances would not be impaired by any obstruction of any character. Its failure to observe that duty and its negligence in placing the wood cart within 42 inches of the track was the primary cause of the accident to Powers and of the consequent liability of Southern Pacific.

It is claimed that the rule in *Erie Railroad Co. v. Tompkins*, 304 U.S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, applies not only to decisions in point but to considered dicta as well. As the portion of the *Layman* decision quoted on page 62 of the Booth-Kelly brief shows, the Oregon court did not stop to inquire whether the agreement if construed to apply to indemnitee's own sole negligence would be valid. Sole negligence is not here involved, and we make no further comment except to

call the court's attention to the general rule stated in 51 C. J., Railroads, Sec. 1314, p. 1185:

"A railroad company may, when acting in its private capacity, relieve itself from an absolute liability imposed by statute for setting fire to property as well as for liability resulting from negligence \* \* \*."

and to point out that such indemnity contracts are recognized by the general law.

*New York Central R. Co. v. Culkeen & Sons Co.*,  
249 Mass. 71, 144 N.E. 96;

*John T. Gorman Coal Co. v. Louisville & N. R. Co.*,  
213 Ky. 551, 281 S.W. 487;

*Terminal R. Assn. of St. Louis v. Ralston-Purina Co.*, 352 Mo. 1013, 180 S.W. (2d) 693;

*Buckeye Cotton Oil Co. v. Louisville & N. R. Co.*,  
24 F. (2d) 347;

*Deep Vein Coal Co. v. Chicago & E. I. R. Co.*,  
71 F. (2d) 963.

Where a contract is involved, as here, the intent of the parties as expressed in that agreement must prevail. As pointed out by the Oregon court in *U. S. F. & G. Co. v. Thomlinson Co.*, 172 Or. 307, 141 P. (2d) 817, an indemnitee may recover despite his own acts if the agreement so provides. In such case, an indemnitee need not go so far as to prove that liability arose from the active or primary negligence of the indemnitor.

The cases cited by counsel on page 68 are not in point. *Johnson Administrator v. Richmond & D. R. Co.*, 86 Va. 975, 11 S.E. 829, involves an exemption contract. It was rejected by the Supreme Court of the United States in *Hartford Fire Ins. Co. v. Chicago M. & St. P. R. Co.*,

175 U.S. 91, 20 S. Ct. 33, 44 L. Ed. 84, and even in Virginia was changed by legislation. See *Aetna Ins. Co. v. Atlantic C. L. R. Co.*, 79 F. (2d) 465.

Other cases there cited illustrate the point that whenever there is a relationship involving public service companies, a bargain exempting the public utility from its duties *as such*, is invalid. These cases do not apply here, because Southern Pacific agreed to services beyond the requirements of the law.

Southern Pacific's right to recover in full is supported by the *Astoria, Thomlinson Co.* and other Oregon cases cited. Since Booth-Kelly's primary responsibility both under contract and independent of agreement has been established, recovery for \$46,568.99 should be granted.

## ANSWER TO BOOTH-KELLY'S SPECIFICATION OF ERROR NO. VI

### Summary of Argument

The trial court's finding that the damage to Powers and the liability of Southern Pacific was the natural and necessary result of Booth-Kelly's breach of the provisions of the spur track agreement relating to impaired clearances, is supported by substantial evidence and should not be disturbed.

The trial court correctly determined that custom varying the provisions of the contract was not proven, and properly concluded there was no waiver of the breach of contract.

It is admitted by Booth-Kelly that the wood cart was placed and left by its employees within 42 inches of the spur track. (T. 34.) This distance is a violation of



the clearance lines prescribed in Section 5 of the agreement (T. 8-10.) By arguing that the cart is not included under the provisions of the agreement, counsel tacitly admits that the actions of Booth-Kelly's employees constituted a breach, if Section 5 applies to the wood cart.

Section 5 provides in part that “\* \* \* no \* \* \* material \* \* \* or obstruction of any character shall be piled \* \* \* stored or maintained” within specified clearance lines. It is clear the cart contained materials. It was an obstruction. It was stored or maintained alongside the track pending use by Booth-Kelly. Witness Nysten testified that the cart was pulled over into position by a tractor or jitney. After being left in position without motive power—as opposed to a Hyster engaged in loading—the cart was as permanent an obstruction as any pile of wood, pipe or poles.

The primary cause of Southern Pacific's failure to provide its employee Powers with a safe place in which to work, and the necessary cause of damage to Powers was the presence of the wood cart. Without its presence, no accident would have occurred.

The trial court correctly found that although employees of Southern Pacific knew of the presence of the wood cart and operations continued thereafter, the loss and damage to Powers were not proximately caused by these conditions (Finding of Fact No. 18, T. 54). The proximate cause as between the parties to this action was the act and omission of Booth-Kelly in placing and leaving the cart. The injury to Powers was the natural result



of placing the cart, and under the spur track agreement Booth-Kelly is answerable for the results of its breach.

Counsel's argument, and the citations made in Booth-Kelly's brief, slide away from the paramount question, that is, the responsibility as between Booth-Kelly and Southern Pacific for the damage to Powers and resulting loss to Southern Pacific, under the agreement.

We have already pointed out that in *Wm. Cameron & Co. v. Thompson*, . . . Tex. Civ. App. . . ., 175 S.W. (2d) 307, the hand truck was under control of the Railroad's employees. In *Central of Georgia Ry. Co. v. Swift & Co.*, 23 Ga. App. 346, 98 S.E. 256, no agreement was cited and no opinion was written. In *Glappa v. Detroit Etc. R. Co.*, 179 Mich. 76, as in *Kanawha Ry. v. Kerse*, 239 U.S. 576, 36 S. Ct. 174, 60 L. Ed. 448, appeals from actions successfully prosecuted by the injured parties were involved.

It is significant counsel cites no Oregon cases in support of his argument. As previously stated, Oregon law supports the contentions of Southern Pacific that the primary responsibility under the agreement rests on Booth-Kelly.

The existence of waiver was not proven by Booth-Kelly and the doctrine has no application under the facts of this case.

Conclusion of Law No. 3, (T. 55);

56 *Am. Jur.*, *Waiver*, Sections 11-17, 22, pp. 112-7;

67 *C. J.*, *Waiver*, Sections 2-8, pp. 294-307.

There is no evidence that Southern Pacific, acting through any agent specifically authorized in the matter,

intentionally and voluntarily agreed to waive damages for breach of contract. The fact that employees continued to operate over the track after the presence of the cart became known does not establish authorization of employees to act or intention to waive by Southern Pacific.

Booth-Kelly has failed in its burden of proof on the subject.

56 *Am. Jur., Waiver*, Sec. 22, p. 123.

Nor is the doctrine of estoppel by custom applicable. As the stipulation between the parties shows (T. 110-11) there is testimony that no employee except the superintendent would have authority to modify the spur track agreement. The fact that the railroad's employees might have notified Booth-Kelly from time to time of pieces of lumber dropped on the track, would not establish a custom that Southern Pacific would always give such notice. In the instant situation, since the cart was placed and left by Booth Kelly's employees within 42 inches of the track, it was presumed they had knowledge, and warning would have been superfluous.

As a matter of law, the parol testimony of Witness Nysten was inadmissible to vary or contradict the terms of the spur track agreement.

2 *Jones on Ev.*, 4th Ed., Sec. 465, p. 887.

In any event, since evidence was introduced through only one witness on the subject, Booth-Kelly has failed to prove this defense.

Section 2-902, O.C.L.A.

**SUMMARY**

Since the placing and leaving of the wood cart was not only in direct violation of contract, but was found to be the primary cause of the damage to Powers and liability of Southern Pacific, Booth-Kelly's primary responsibility for the accident, as between the parties to this action is established. Southern Pacific is entitled to recover the full amount, \$44,699.46 judgment costs and \$1,869.53 costs and attorney fees.

Respectfully submitted,

KOERNER, YOUNG, SWETT & MCCOLLOCH,  
JAMES C. DEZENDORF,  
ALFRED H. CORBETT,

*Attorneys for Cross-Appellant  
and Appellee.*

No. 12340

In The

**United States Court of Appeals  
For the Ninth Circuit**

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Appellee,*

and

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Appellant,*

vs.

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Appellee.*

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**Combined Brief of Cross-Appellee and  
Appellant Booth-Kelly Lumber Company**

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**BRIEF OF CROSS-APPELLEE**

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Appeal and Cross-Appeal from the United States District  
Court for the District of Oregon.

HONORABLE JAMES ALGER FEE, *Judge*

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KOERNER, YOUNG, SWETT & McCULLOCH,

JAMES C. DEZENDORF,

ALFRED H. CORBETT,

800 Pacific Building, Portland, Oregon,

*Attorneys for Appellee.*

VEAZIE, POWERS & VEAZIE, and

JAMES ARTHUR POWERS,

622 Lumberman's Building, Portland, Oregon,

*Attorneys for Appellant.*

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**PAUL E. O'BRIEN,**

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No. 12340

In The  
United States Court of Appeals  
For the Ninth Circuit

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BOOTH-KELLY LUMBER COMPANY, a Corporation, *Appellant*,  
vs.

SOUTHERN PACIFIC COMPANY, a Corporation, *Appellee*,  
and

SOUTHERN PACIFIC COMPANY, a Corporation, *Appellant*,  
vs.

BOOTH-KELLY LUMBER COMPANY, a Corporation, *Appellee*.

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**Combined Brief of Cross-Appellee and  
Appellant Booth-Kelly Lumber Company**

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**BRIEF OF CROSS-APPELLEE**

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Appeal and Cross-Appeal from the United States District Court  
for the District of Oregon.

HONORABLE JAMES ALGER FEE, Judge.

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(Appellant in this cross-appeal is referred to herein  
as "Southern Pacific" or "railroad" and appellee is re-  
ferred to as "Booth-Kelly.")



**ANSWER TO THE SOUTHERN PACIFIC'S  
SPECIFICATION OF ERROR NO. 1  
SUMMARY OF ARGUMENT**

**POINT ONE:** There was no breach of Section 5 of the industrial track agreement relating to clearances.

**POINT TWO:** The Oregon statutes as to spur track service are controlling in this case, and since they require the service provided for by the spur track agreement there was no consideration for such contract.

**POINT THREE:** The cause of the injury was not any allegedly impaired clearance but the railroad's subsequent intervening independent negligence in failing to warn its employee and in continuing operation on the obstructed track.

**POINT FOUR:** If there was a breach, the Southern Pacific can claim no benefit thereby since it had waived any breach and was in any case estopped by its failure to conform to the custom which had grown up regarding the removal of obstructions.

**POINT FIVE:** Since the contract contained several express indemnity clauses, the railroad cannot recover indemnity based on any implied contract of indemnity for breach since no clause can be implied when the parties have expressly contracted on the matter nor will such a contract be construed to cover the railroad's own negligence.

**POINT SIX:** A breach, if any, of the agreement as to clearances would not in any event give rise to a cause of action for any damages resulting therefrom since Section 9 of the agreement expressly provides that railroad shall have a right to discontinue service in that event.

**POINT SEVEN:** The agreement gave the railroad full control of the track and therefore the railroad had the right to remove a cart left near the track if it was dangerous to operations thereon, irrespective of the ownership of the obstruction.

**POINT EIGHT:** Since the railroad seeks damages for an alleged breach of contract, the proper measure of such damages is not tort damages or costs to which the railroad was subjected to for its own independent act of negligence.

### **ARGUMENT**

The Southern Pacific contends that there was a breach of the impaired clearance provisions of the industrial spur track agreement. At page 69 of Booth-Kelly's opening brief, Booth-Kelly has specified as error two of three Findings of Fact relied on by the Southern Pacific under its present Specification of Error. (No. 21, 13) (T 53-54). In support of Booth-Kelly's specification of error referred to, it was argued that: "there was no

breach of the spur track contract relating to clearance.” (Brief 70-72) That argument is still relied on to meet the contention of the Southern Pacific here that there was no breach. Essentially there was no breach because a moveable lumber cart was not covered by impaired clearance language which related to fixed obstructions like pipes or poles.

The Southern Pacific next states that as a common carrier it was not compelled under the Interstate Commerce Act to render service to Booth-Kelly over the industrial spur, citing 49 U.S.C.A. Sec. 1 (9). Its title is *Switch connections and tracks*, and it provides that under certain conditions a carrier subject to the act must construct and operate switch connections with side tracks. (Section 1 (9) is set out in the Southern Pacific’s Brief at page 36.)

That section should be compared with 49 U.S.C.A. 1 (22) *Construction, Etc., of Spurs, Switches, Etc., within State*:

“The authority of the commission conferred by paragraphs (18) to (21), both inclusive, shall not extend to the construction of spur, industrial, team, switching, or side tracks, located or to be located wholly within one State, \* \* \*”

Section 1 (9) is not in point here because it refers to the provision of a *switch connection* to a railroad line

and not with the provision of *spur track service*. For example, under this section a railroad cannot be ordered to build a switch connection with shipper's side track until after the shipper has built such side track. *Cleveland, C.C. & St. L. Ry. Co. v. U.S.*, 275 U.S. 404, 413, 72 L. Ed. 338, 48 S. Ct. 189.

A quotation from the Cleveland case, *supra*, makes clear the relationship of the two sections:

"In denying their application to side tracks or spurs, paragraph 22 refers to tracks built by the carrier as part of its railroad. (Citation) Paragraph 9, on the other hand, relates to switch connections with private sidings built by the shipper." (P. 408)

Here the Southern Pacific did build the spur in question. Section 13 of the spur track agreement provides that the railroad at its own expense will maintain the track (T 17); by Section 8 it may rearrange, reconstruct, or modify the elevation of the track (T 12); and Section 4 provides that: "\* \* \* said Track shall be under control of Railroad and Railroad shall have right to use same when not to the detriment of the Industry." (T 8) All these facts make it clear that the spur was built and operated as part of the railroad; it was not simply a question of a connection.

Therefore, 49 U.S.C.A. 1 Sec. (22) is controlling here. Since it is controlling, *Luton Mining Co. v. Louisville N. R. Co.*, 276 Ky. 321, 123 S.W. (2d) 1055, inter-



preting Section 1 (9) is not in point here. On pages 38 through 51 of Booth-Kelly's opening brief, Section 1 (22) is analyzed and Oregon statutes cited which show that spur track service is compulsory and therefore no consideration existed for any contract with the Southern Pacific as to indemnity. Secondly, there was no consideration because the indemnity section was inserted in the Revised Spur Track Agreement without new consideration after long operation under contracts having no such clause. (Opening brief 51-53).

To summarize, Booth-Kelly denies liability for breach of the clearance provisions of the industrial spur track agreement because: (1) there was no breach; (2) there was no valid contract since no consideration moved to Booth-Kelly; and (3) the cause of the injury was not the proximity of the cart to the track since the railroad's subsequent intervening independent negligence, namely, a failure to warn and continuation of operations on an obstructed track, was the proximate cause. That argument is set out in detail at pages 72 to 76 of Booth-Kelly's opening brief in support of the following point: "If there was a breach, appellee's loss did not result from the alleged breach." (See also Booth-Kelly's opening brief: pages 32-34; pages 29-32.)

A fourth reason the Southern Pacific can not recover is that assuming *arguendo* there was a breach, the rail-



road waived any breach and hence cannot now claim damages. The court below found that the railroad's employees observed the position of the cart and operations continued thereafter prior to the accident. (T 54) The argument is made in detail in Booth-Kelly's opening brief (p.p. 76-77). Finally, the Southern Pacific cannot recover for any breach of the contract because it is estopped by reason of its failure to conform to a custom which had grown up governing the removal of obstructions. (Opening brief pp. 77-79).

Other reasons exist for denying recovery for breach of contract. Here the contract contained several express indemnity clauses: Sections 7 and 18. (T. 11, 19). If indemnity is sought for breach of contract they must control because they represent the express contract of the parties on this matter. No contract can be implied to cover matters on which the parties have expressly contracted. *Failing v. Osborne*, 3 Or. 498. Therefore, an attempt to recover for breach of contract without invoking the indemnity clauses contained in that contract must fail. Recovery on an implied contract of indemnity is especially difficult since the court below concluded as a matter of law that Booth-Kelly was not obliged to pay the railroad \$44,568.99 or any part thereof, *independent of the spur track agreement*. (Conclusion No. 5, T. 55).

Even if the railroad could rely on an implied indemnity contract, such a contract will not be construed to cover its own negligence. *U. S. Fid. & Guar. Co. v. Thomlinson Co.*, 172 Or. 307, 324, 141 P. 2d 817. Here the railroad was found negligent. (Finding of Fact No. 14, T. 54). Nor will contribution allow the railroad recovery here. First, it sues for breach of contract not for sharing tort damage. Second, there is no contribution between tortfeasors in Oregon. *Fidelity & Casualty Co. v. Chapman*, 167 Or. 661, 120 P. 2d 223.

Another reason exists against implying a contract of indemnity: Section 9 provides a specific remedy for any alleged obstruction of the track. (T. 13). That section allows the railroad to discontinue service in such case. Since the contract has set out the specific remedy, it must be deemed exclusive, and therefore no cause of action for damages can accrue. To hold otherwise would be to allow the railroad to create a cause of action by its own failure to exercise its contractual remedy where as here the railroad knew of the obstruction long before the accident. (T. 54).

Again the agreement gave the railroad full control of the track: Sections 4 and 8. (T. 8, 12). The track is broadly defined. (T. 6). Therefore, the railroad would have a right and a *duty* to remove dangerous obstructions irrespective of the ownership of such obstructions

just as it would on its main line. This track served several other industries and was used for general switching purposes. (T. 89, 105). At the time of the accident the railroad was serving one of these other industries as the agreement provided. (T. 90, 8). The spur track was therefore in effect part of the Southern Pacific system which in fact owned it. (T. 104). What would be allowable on the main line should therefore be allowable here especially since the agreement fails to provide for the removal of obstructions which it prohibits.

The railroad does not seek damages for breach of contract which would presumably be the cost of removing the obstruction but the amount for which it was held liable for its own tort, a failure to provide a safe place to work. The proper damages are those necessary to restore the track to the status quo, not those necessary to reimburse the railroad for its independent breach of duty to its employee. Not only were the damages caused by the railroad's independent negligence but they were not such as Booth-Kelly was legally obliged to envision as consequences of any alleged breach.

Any causal connection of an alleged breach of contract is broken by the long time intervening between the cart being left and the accident, and by the independent negligence of the train crew, particularly the con-

ductor, and the negligence of the injured man. Even if some negligence of industry concurred to produce the injury, to allow recovery as contract damages of the full amount of the railroad's tort liability would be unreasonable and would in effect defeat the well settled Oregon rule that contribution will not be enforced between tortfeasors. *Fidelity & Casualty Co. v. Chapman, supra*. Finally, since recovery is here sought for breach of contract and not indemnity, the expenses incurred in the Powers action are not a proper part of the damages caused by the breach of contract since quite apart from any contract the railroad would have been obliged to defend such an action against it as an employer under the Federal law.

**ANSWER TO THE SOUTHERN PACIFIC'S  
SPECIFICATION OF ERROR NO. 2, POINT ONE  
SUMMARY OF ARGUMENT**

**POINT ONE:** The Southern Pacific relies on two indemnity sections in the spur track agreement: Section 18 and the second paragraph of Section 7; but only Section 7 is in point here.

**POINT TWO:** In the second paragraph of Section 7, there are two separate and distinct indemnity clauses and the Southern Pacific bases its argument only on the one relating to an act or omission of Booth-Kelly



and not on the one relating to joint and concurring negligence.

**POINT THREE:** An application of the principles of *res judicata* to *Powers v. Southern Pacific Company* shows that the railroad was held liable there only for its own act, a failure to warn, and not for any act or omission of Booth-Kelly as required by Section 7.

**POINT FOUR:** There is no ambiguity in the interpretation of the second paragraph of Section 7. But *Southern Pacific Company v. Layman*, an Oregon authority on interpretation of indemnity agreements, supports the contention of Booth-Kelly by its holding, while the dicta relied on by the railroad is not adverse to Booth-Kelly.

**POINT FIVE:** The Southern Pacific in its argument recognizes that the first judgment is *res judicata* against the parties here, and therefore its reliance on certain findings of fact as proximate cause is misplaced since the application of the doctrine of *res judicata* to the prior action makes those findings erroneous.

**POINT SIX:** The case of *Astoria v. Astoria & Columbia R. Co.*, is not authority for Southern Pacific's claim for recovery under the spur track agreement.

### **ARGUMENT**

The Southern Pacific here relies on two sections of its



spur track agreement dealing with indemnity: Section 7 and Section 18. (Brief 11). A reading of Section 18 shows that it is not in point here. It only extends to:

“\* \* \* all liability resulting from the movement of cars and/or operations by Industry upon said tracks.” (T. 19).

The qualifying phrase “by Industry” modifies movement of cars. This is especially obvious when the phrase “upon said track,” which follows the phrase “by Industry” is considered. The phrase “upon said track” must modify “movement of cars” since there is no other place on which they could move. To say that “by Industry,” a small phrase sandwiched in between, does not refer to “movement of cars” is then particularly difficult. The phrase “by Industry on said track” is a unit which modifies both “movement of cars” and “operations,” and the unit phrase has no application here since the accident occurred when the Southern Pacific and not Booth-Kelly was moving cars on the track.

The accident occurred on the part of the track shown by the solid red line on the blueprint attached to Exhibit 1. (T. 103-4). Paragraph 16 of the spur track agreement provides as to such track that industry may move cars itself in certain ways. (T. 18). The function of Section 18 then is to protect the railroad against such operations by industry.

Furthermore, both Section 18 and Section 16 were included in the same typewritten supplement to the contract and therefore were conceived together, and hence should be construed together. Section 19 is included in the same typewritten supplement immediately following the special indemnity section and helps to resolve any possible ambiguity in that section since it provides in effect that Industry may have to move cars itself on certain portions of the track. (T. 19). Therefore, Section 18 must be understood as removing liability from the Railroad for operations *by Industry* on the track and not for the Railroad's own operations.

The problem here is then the proper interpretation and application of Section 7, more exactly the second paragraph in Section 7. (T. 11). This second paragraph breaks down into two distinct parts: first: Industry agrees to hold the Railroad harmless for any act or omission of Industry; second, in case of any non-fire liability arising from the joint and concurring negligence of the two parties, such liability is to be borne equally.

Booth-Kelly contends that the second part of the indemnity paragraph making both parties equally liable for their joint and concurring negligence is the only part of Section 7 which may conceivably be in point.

But in its opening brief, Booth-Kelly has argued in detail that even this second clause as to joint negligence is not applicable here. (Brief 21-29). The Southern Pacific in its Specification of Error No. 2, takes an alternative position, arguing the court erred in failing to enter judgment for the appellant for \$46,568.99, due to an act or omission of Booth-Kelly or in the alternative that judgment for \$23,284.49 should have been entered as one-half the loss suffered by the railroad by reason of an act or omission of Booth-Kelly. (Brief 9). This last alternative is a hodge-podge. For, if an act or omission of Booth-Kelly caused damage, the railroad is entitled to recover all its loss, not just half. If it is entitled to recover only half, it must be guilty of joint and concurring negligence.

Although the Southern Pacific states two alternative specifications under Specification of Error No. 2, both based on an act or omission of Industry. Point Three of the Southern Pacific's specification of error in fact argues that the joint and concurring clause does not apply here. Since the Southern Pacific makes no argument that the joint clause is applicable, Booth-Kelly relies on the argument set out in detail in its opening brief, that the joint clause is not applicable here. (Brief 21-29).

The only language of Section 7 then, which may be

in point here, may be summarized as follows: The Railroad must be indemnified for loss caused by act or omission of Industry. But that part of Section 7 does not apply to the facts of this case. Booth-Kelly so argued in detail in its opening brief. (pp. 21-29). In summary form that argument is that the application of the principles of *res judicata* to *Powers v. Southern Pacific Company* shows that the railroad was held there *solely* for its failure to carry out its statutory duty as employer to warn its brakemen of unsafe working conditions, and not for any negligence in leaving the wood cart near the tracks which would be an act or omission of Booth-Kelly within the meaning of this clause. In short, the railroad can not claim indemnity for its own failure to warn since the clause requires an act or omission of Booth-Kelly. Booth-Kelly did leave the cart; but the railroad was not held for that act and therefore cannot demand indemnity for it.

Here the loss caused to the railroad was by its own act not by any act or omission of Booth-Kelly. It is immaterial that the wood cart was under the control of Booth-Kelly, a fact which may help to construe ambiguous language. Here the language is not ambiguous; it leaves no doubt that Booth-Kelly was to indemnify for only two things: (1) loss caused to the railroad by its own act or omission; and, (2) half of the liability caused by joint negligence. (This last as has been pointed, is



not argued here by the railroad and is hence excluded from consideration.)

Booth-Kelly, therefore, does not need to assert the undisputed law in Oregon that an indemnity provision will not be construed to cover losses caused by indemnitee's own negligence unless such intention is expressed in clear and unequivocal terms. *Southern Pacific Company v. Layman*, 173 Or. 273, 145 P. 2d 295.

Although the Southern Pacific recognizes that the general impact of the Layman decision, *supra*, is against its position, nevertheless it attempts to gain support from certain language of court at page 282. (Brief 16). A reading of the quotation and the case shows it is no comfort to the railroad. The quotation in effect states if the party contracting with the railroad has a duty his negligent failure to discharge that duty might be the primary cause of an accident. Here Booth-Kelly denies that it had a contractual duty to keep the track clear of wood carts for 42 inches; in short, the wood cart was not one of the prohibited obstructions to clearance. The argument as made in detail in the opening brief, (pp. 70-72) and will not be repeated here. Nor, as will be shown, was any act of Booth-Kelly the primary cause of the accident here.

Finally, other distinctions exist. The agreement subject matter there is different involving a crossing rather



than a spur track. The indemnity clause there was significantly broader than the clause here. Despite the much broader character of the indemnity clause there the court held that the Southern Pacific could not recover indemnity for payments made because of its sole negligence. Here the clause is clear, saying simply "act or omission of Industry," yet again the Southern Pacific seeks to recover thereunder for its sole negligence, a failure to warn.

The Southern Pacific relies on several Findings of Fact made by the court below; particularly reliance is on Finding of Fact 9 and 10, (Brief 12). Those two findings are specified as error in Booth-Kelly's opening brief at page 21. The argument there is based on *res judicata*; the contention is that if the principles of *res judicata* are applied to *Powers v. Southern Pacific Company*, it is now *res judicata* that the railroad's negligence was the immediate proximate cause of the accident and injury. The argument is developed in detail in Booth-Kelly's opening brief. (pp. 32-37).

Closely analogous cases on the facts are cited there to support Booth-Kelly's contention that the proximate cause of the accident was the railroad's failure to warn its employee. *Wm. Cameron & Co. v. Thompson*, Tex. Civ. App., 175 S. W. 2d 307, (unblocked hand truck); *Central of Georgia Ry. Co. v. Swift & Co.*, 23 Ga. App.

346, 98 S.E. 256, (unlighted shed near tracks); *Glappa v. Detroit, Etc., R. Co.*, 179 Mich. 76, 146 N.W. 134, (sand on track). Here the Southern Pacific is content with unsupported assertions that:

“ \* \* \* Booth-Kelly’s affirmative act of placing the cart and leaving it in position caused the accident.” (Brief 13).

Or it assumes its case by asserting it was established that:

“ \* \* \* Powers was injured by a wood cart which Booth-Kelly placed \* \* \* ” (Brief 12).

The very question at issue before this court is who as a legal matter caused this accident. Yet the Southern Pacific states as a conclusion that he was injured by a wood cart, as if that settles who was responsible for the injury.

The Southern Pacific asserts that its only fault was the constructive failure to do its duty imposed by statute. (Brief 12-13). Yet as has been explained in Booth-Kelly’s opening brief: to switch on an obstructed track is itself negligent if the railroad employees know of the obstruction. (Brief 75). *Kanawha Railway v. Kerse*, 239 U.S. 576, 579, 36 S. Ct. 174, 60 L. Ed. 448. It is difficult to see that an error of omission is necessarily any less grave than an error of commission. But if that distinction is to be drawn and adopted, the railroad was

guilty of a positive error of commission when it operated on the obstructed track.

The Southern Pacific in its answering brief seems to adopt Booth-Kelly's contention as to the principles of *res judicata*. One of the main authorities for the proposition that the first judgment is conclusive on the parties to the second action is *Astoria v. Astoria & Columbia River R. Co.*, 67 Or. 538, 136 Pac. 645. The Southern Pacific cites that case and acknowledges that the scope of the estoppel by judgment in the primary case embraces all the issues determined by it, although the proposition is stated as related to only that case. (Brief 15). Since the railroad acknowledges the application of *res judicata* here, its reliance on findings of the court below is misplaced. Those findings are error because as authorities cited show the facts established in the first action determine that the railroad's negligence was the proximate cause of the accident.

The *Astoria* case, *supra*, is still relied on by Booth-Kelly but the pertinence of the authority to the case at bar is in regard to *res judicata* and estoppel, not as to substantive law of indemnity and negligence. Specifically, it is not as the Southern Pacific states:

"\* \* \* direct authority for Southern Pacific's claim for full recovery under the spur track agreement." (Brief 14).

Parenthetically it may be stated that the Astoria case, *supra*, does not justify recovery of costs and attorneys fees here because the carefully drawn contract here does not provide for such in its enumeration of coverage while in the Astoria case, *supra*, there was no such contract.

The Astoria case, *supra*, cannot be direct authority for recovery under the spur track agreement because in that case there was no express indemnity contract. The only "contract" there was an ordinance granting a franchise which merely required the railroad company to lay its track rails even with the grade of the elevated street and to keep the street crossing in good condition and repair. (pp. 543, 548).

The Court in the Astoria case, *supra*, concludes its analysis by stating that a non-observance of the ordinance provisions was proximate cause of the accident. (P. 548-9). In short, there the city as indemnitee was able by virtue of its municipal powers to delegate the duty of keeping the street crossing in repair. Here the indemnitee is the Southern Pacific and it cannot delegate its statutory duty to warn under the Federal Employer's Liability Act to Booth-Kelly. Here Booth-Kelly agrees that a non-observance of these provisions (employer's duty to warn) was the proximate cause of the accident.

Finally, the Southern Pacific quotes from the Oregon court's analysis of the Astoria case, *supra*, made in *Fidelity and Casualty Co. of N. Y. v. Chapman*, 167 Or. 661, 120 P. 2d 223 (Brief 15). That quotation is in part:

"The City was held liable by reason of its failure to *enforce an ordinance* requiring the company to repair the defect." (Emphasis supplied)

Here the Southern Pacific in *Powers v. Southern Pacific Company*, was not held for any secondary liability, failure to enforce an ordinance, but for its own failure to meet a primary statutory obligation imposed on railroad employers by Federal law.

Even if the Astoria case, *supra*, is in point it affords no comfort to the railroad. In that case, the court's method of ascertaining whose negligence was active or passive is to analyze the complaint in the first action. (p. 547-8). Therefore the complaint in *Powers v. Southern Pacific Company* must be examined here. (Ex. 2a). Its effect is summarized in the Pre-Trial Order as follows:

"The complaint alleged breach of Southern Pacific Company's statutory duty of using ordinary care to provide said Mack D. Powers with a reasonably safe place in which to work in that, first, it caused and permitted the wood cart to remain on the track, and second, it failed to warn him of the presence of the wood cart and the resultant insufficient clearance." (T. 34-5).



Thus it may be seen that the Southern Pacific was in fact charged with active negligence; a breach of its statutory duty to warn. The negligence, if any, of Booth-Kelly, merely was suffering a condition to exist upon which the active negligence of the railroad operated. Thus applying the test of the Astoria case, active or passive negligence, by the method of the Astoria case, analysis of the complaint in the first action, the conclusion reached is that here the railroad was guilty of active negligence.

Thus the general statements in the Astoria case on which the Southern Pacific is content to rest its case do not support its contention that Booth-Kelly is liable here by being actively negligent. Furthermore, the Astoria case is not so similar factually as authorities cited by Booth-Kelly in its opening brief and again here: Cameron case, *supra*, Central of Georgia case, *supra*; and, Glappa case, *supra*. These cases all deal with injuries caused by obstruction to spur tracks and not with a pedestrian falling from an unguarded apron leading up to a railroad track located in a city street. (The statement of the facts in the railroad's brief at page 14 is garbled.)

In its opening brief Booth-Kelly made these cases the basis of a detailed argument that the active cause of the accident was the Southern Pacific's failing to

warn its employee and in continuing operations on an obstructed track. *Kanawha Railway v. Kerse*, 239 U.S. 576, 579, 36 S. Ct. 174, 60 L. Ed. 448. (Brief 72-76; 32-35). Booth-Kelly relies on the arguments there advanced, but as a summary quotes from the Central of Georgia case, *supra*, which succinctly disposes of the Southern Pacific's contention that it was here guilty of only passive negligence. In that case the railroad had also failed to warn an employee of danger on a spur track and had continued to operate on the track despite its knowledge of the dangerous condition thereon. The court states:

“The act of the railroad company in this voluntarily operating its train along said private track and under said shed, and in such undisproved negligent manner did not amount to *mere legal, passive acquiescence in the negligence of the oil company* in maintaining the shed in a dangerous condition, but *such active, positive and negligent conduct on the part of the railroad* itself amounted to an actual participation by it in the *proximate* cause of the homicide.” (Emphasis supplied) (P. 256)

Parenthetically, it may be stated that Booth-Kelly relied on these four authorities in its opening brief. (pp. 32-34; 72-73). In its answer the Southern Pacific attempts to distinguish those cases. The distinctions attempted are faulty, but will be answered now to prevent any doubt as to the validity of the authorities above

cited. First, the Central case, *supra*, is distinguished by asserting that no indemnity contract was involved. (Brief 34, 50). At the places where the Southern Pacific attempts to distinguish that authority and also here the lack of an indemnity contract is immaterial since the authority is cited only on the question as to which of the parties was primarily negligent and not as to who contracted to bear the ultimate burden. The Southern Pacific seeks to disparage the case as an authority by saying no opinion was written. That is a quibble because as the official report shows, Jenkin, J. prepared a lengthy syllabus for the court in which he even cites a case.

The Cameron case, *supra*, is distinguished by Southern Pacific because no breach of contract is involved. The answer that has just made in conjunction with the Central case, *supra*, applies here. Second, it is said that there the hand truck was under the control of the railroad's employees. But there is no showing in the case that the train crew there had any more right to move the hand truck than they did the cart here. As for the truck being in the freight car, the car was presumably rented to the warehouse company since it had been hired to haul freight. The train crew had no business inside of the freight car there since any accident could have been avoided by shutting the car door. In short, the Southern Pacific

is attempting to draw a distinction between the inside of a rented freight car where the trainmen had no business, and the edge of a railroad right-of-way where the track was owned by railroad but the ground through which it ran was leased by the railroad to Booth-Kelly. (Blueprint attached to Ex. 1; T 103-4). There seems little distinction; in neither case did the trainmen have a right to move the cart or the hand cart. In both cases the trainmen, by simple precautions, could have avoided the accident: there, by closing the door, and here by requesting the cart moved.

Finally, the Glappa case, *supra*, is distinguished as merely involving the liability of the railroad to a teamster or merely the appeal of the injured person involved. (Brief 34, 50). The Kanawha Ry. case, *supra*, is also distinguished as involving merely the appeal against a recovery of the injured party. (Brief 50). That is admitted, but the reason these cases are cited here and in the opening brief (p. 34, 73) is that they analyze the negligence involved in similar fact situations. In the Glappa case, *supra*, it was urged as error that the evidence did not show negligence on the part of the defendant railroad. (p. 79). The court then points out that despite a third party's duty to remove the sand, that: "It was the alleged negligent movement of the cars over the accumulated sand which caused the injury." (P.



80). That is the point of the Glappa case, *supra*, for the case at bar. The Kanawha case, *supra*, shows that as a matter of law the Southern Pacific was actively negligent in knowingly continuing to operate on an obstructed track. It is immaterial that different type parties are involved here because that does not change the classification of certain acts or omissions as negligent.

To summarize, the cases relied on by Booth-Kelly not only are the most closely analogous factually but they are not distinguishable from the case at bar as to the points for which they are cited.

**ANSWER TO THE SOUTHERN PACIFIC'S  
SPECIFICATION OF ERROR NO. 2, POINT TWO  
SUMMARY OF ARGUMENT**

Southern Pacific's contention that the Pre-trial Order is deficient in pleading certain elements of negligence is based upon an Oregon decision, but in the Federal courts, pleading is controlled by the Federal Rules of Civil Procedure. Federal decisions show that the Pre-Trial Order was an adequate pleading on this point; but in any case the Pre-Trial Order is adequate to meet the requirements of the state authority cited.

**ARGUMENT**

The Southern Pacific, without specifically so stating, contends that state law controls the determination of



this pleading point by citing *Fehely v. Senders*, 170, Or. 457, 135 P. 2d 283, without comment and by basing Point Two on its holding, but it is well established that:

“The Federal Rules of Civil Procedure, 28 U.S. C.A. following Section 723c, govern pleading, practice, and procedure in the courts of the United States.” *Ettman v. Federal Life Ins. Co.* 137 F. 2d 121, 127; *Moore v. Illinois Central R. Co.*, 24 F. Supp. 731, 733, *aff’d* 312 U.S. 630, 85 L. Ed. 1089, 61 S. Ct. 754.

Rule 8 (f) provides that: “All pleadings shall be so construed as to do substantial justice.” To that end the pleading should be viewed in the light most favorable to its drafter. *Ivaneik v. Wright Aeronautical Corporation*, 68 F. Supp. 270, 272.

But the Southern Pacific now contends that it was error for the court to reduce the recovery granted upon the basis of Finding of Fact No. 15 that: “Some elements of negligence on the part of the plaintiff concurred to cause the accident.” (T. 54). That was error it is contended, because the Finding of Fact was not anticipated in the pleadings, that is, the Pre-Trial Order. It was not anticipated it is claimed because those elements of negligence of which the court found the plaintiff guilty were not specifically charged in the Pre-Trial Order.

But under the federal practice it was not necessary

to specify the precise elements of negligence, a general charge of negligence is sufficient. *Hardin v. Interstate Motor Freight System, Inc.*, 26 F. Supp. 97. In the cited case the court went even further and sustained a motion to strike allegations which were in the nature of specifications of negligence in addition to the general allegation of negligence.

Here there can be no question but that the general question of concurrent negligence was clearly and properly raised in the Pre-Trial Order. For example the following quotations are from the Issues of Fact:

- “4. Did the damage to Plaintiff’s employee arise from the joint or concurring negligence of plaintiff and defendant?” (T. 45).
- “9. Is plaintiff barred from recovering under the track agreement by reason of its own acts and conduct?” (T. 46).

The same point is explicitly raised in the last sentence of C(4), Contentions of the Parties. (T 44) Finally the same point is raised in: Issue of Fact No. 7 (T 45); Contentions of the Parties A(3), T. 38; B(1), T. 40; C(2), T. 42.

But the Pre-Trial Order goes further and meets Southern Pacific’s objection based on the non-applicable state case even more precisely. Contentions of the Parties C(3) states:

“That if it should become an issue under any of Plaintiff’s contentions as to whether plaintiff’s negligence caused the loss and injury to Mack D. Powers or whether plaintiff’s negligence was a contributing cause of said injuries and loss, defendant then contends the railroad was negligent in the following particulars:”

(Then follow nine separate allegations of various states of fact constituting negligence) (T 42-43).

See also the following places where the Contentions of the Parties in the Pre-Trial Order, set out elements of Southern Pacific’s negligence which Southern Pacific now contends was not alleged. (A (2), T 37; B (6), T 41; C (1), T 42).

So far it has been demonstrated that Finding of Fact No. 14 had a basis in pleadings or issues framed by the Pre-Trial Order. Even without the pleadings the course of the trial is adequate to show that the Southern Pacific had an opportunity to answer a charge of concurrent negligence. Rule 15 (b). Here in the course of the trial the precise elements of plaintiff’s negligence were raised and considered and the Southern Pacific did not object. (See T. 61-62; 65-69; 72; 76-77; 112).

**ANSWER TO THE SOUTHERN PACIFIC'S  
SPECIFICATION OF ERROR NO. 2, POINT THREE  
SUMMARY OF ARGUMENT**

**POINT ONE:** Booth-Kelly agrees that the language of the second clause in the indemnity provision relating to concurring negligence does not apply here, but for different reasons than those advanced by the Southern Pacific.

**POINT TWO:** Deep Vein Coal Co. v. Chicago & E. I. R. Co. is not authority for here refusing to apply the concurring negligence clause, and no authority is cited for refusing to give that clause its natural interpretation.

**POINT THREE:** The fact that Booth-Kelly was not primarily negligent prevents the application of the Deep Vein dicta in any case.

**ARGUMENT**

Booth-Kelly contends in its opening brief and still contends that the concurring negligence clause has no application to the case at bar. To that extent Booth-Kelly agrees with Point Three of the Southern Pacific's argument here, but reaches that conclusion by a different route.

First, an analysis of the wording of the clause shows

that it has no application here. The words are "joint or concurring negligence." The negligence of the parties here was obviously not joint negligence, nor was it concurring negligence. *Salt River Valley Water Users' Ass'n. v. Cornum*, 49 Ariz. 1, 4-10, 63 P. 2d 639.

In that case it was held that the negligence of a pole owner in leaving the end of a pole's guy wire projecting, was merely passive and innocuous when a guy wire end caught a pedestrian as he sought to escape the approach of a negligently operated automobile. The court states as page 10:

"Further, it is practically universally held that where one negligence consists merely in creating and maintaining of a passive condition which is innocuous except through and by active negligence on part of a third person, the two are not concurrent. (Citations)."

Here, the proximity of the cart to the track like the hanging guy wire was innocuous except for the active negligence of the railroad in operating on the obstructed track and in failing to warn its employee of a dangerous working condition.

The second reason the concurring negligence clause is not applicable here, are the facts of this case as settled by the application of principles of *res judicata* to *Powers v. Southern Pacific Company*. In that case, recovery was had against the railroad for breach of its *sole* and *non-*



*delegable* duty to warn its employee of a dangerous working condition. In short, the Southern Pacific was held for an independent act of negligence, a failure to warn. The argument is set out in detail in Booth-Kelly's opening brief: pages 22-37; especially pages 26-28 and 31-32.

The third reason the concurring negligence clause is not applicable to the case at bar is that the clause is not sufficiently explicit under the Oregon law to cover the Southern Pacific's own sole negligence. *Southern Pacific Co. v. Layman*, 173 Or. 275, 145 P. 2d 295.

For these reasons the concurring negligence clause is not applicable to the case at bar; and as has been previously pointed out the act or omission clause is not applicable either. By arguing that the concurring negligence clause is not applicable the railroad concedes that its only indemnity clause basis of recovery is the act or omission clause. It thereby repudiates the basis of its recovery in the original action in the court below.

If this court should find that the concurring negligence clause is in point, no basis exists for giving the clause the restricted meaning contended for by the railroad. *Deep Vein Coal Co. v. Chicago E. I. R. Co.*, 71 F. 2d 963, holds only that where there was specific indemnity paragraph dealing with fixture obstructions that such paragraph controls when a pole obstruction

was involved. The paragraph in that case which is similar to Section 7 here was not involved, and statement relied on by the railroad is a gratuitous dicta.

The clause here says:

“\* \* \* joint or concurring negligence of both parties  
\* \* \*” (T. 12).

To say that this phrase does not cover the case where one party is primarily negligent is to rewrite the contract of the parties by importing restrictions not present in the language used by the parties. It is an unnecessary refinement not called for by the words used.

If this court were to find that the concurrent negligence clause is in point, and further that the *Deep Vein* case represents the proper interpretation of that clause, still there is no reason for not applying the clause. To apply the *Deep Vein* formula requires that the negligence of the railroad be consequent upon a primary negligence of Booth-Kelly. Therefore, the Southern Pacific must argue Booth-Kelly's negligence is primary.

Presumably, that argument is based on the Astoria case, *supra*. In answer to Point One under Southern Pacific's Specification of Error No. 2, it has been pointed out in great detail why that case does not demonstrate by analogy that the negligence of Booth-Kelly was primary. In addition as has been pointed out the fact that the indemnitee there was a municipality had an im-

portant effect in determining that the indemnitee's negligence in that case of secondary.

There is another reason still why Booth-Kelly's negligence here was not primary. *Leavitt v. Stamp*, 134 Or. 191, 293 P. 414, involved the question of a safe place to work. The court states at page 196:

"In regard to an intervening, efficient, proximate cause, in such cases it may be stated that a prior and remote cause cannot be made the basis of an action for negligence, if such remote cause did nothing more than furnish the condition or give rise to the occasion by which the injury was made possible, if there intervened between such prior or remote cause and the injury a distinct, successive, unrelated and efficient cause of the injury, even though such injury would not have happened but for such condition or occasion. If no danger existed in the condition, except because of the independent cause, such condition was not the proximate cause: 45 C. J. 931, § 491."

It is submitted that the facts here meet the requirements of the Oregon court. Here no danger existed except by reason of the independent cause, Southern Pacific's failure to warn. This is evident from the fact that trains had been switched in and out several occasions for over a week while the cart was near the track without anyone being injured. (Reporter's Transcript, *Powers v. Southern Pacific Company*, p. 20, 83-84; see opening brief p. 73-74). On this particular trip no one

else was hurt; it may be conjectured because all the other crew members knew of the cart's location. (Reporter's Transcript, *supra*, p. 283-4; 306). Second, *Wm. Cameron & Co. v. Thompson, Tex. Civ. App.*, 175 S.W. 2d 307, with like factual circumstances is specific authority for asserting that Booth-Kelly was not required to anticipate that the railroad would proceed to negligently switch on the obstructed track without warning its employee. (See also opening brief pp. 32-37). Finally, the whole question of proximate or primary cause is argued in detail in Booth-Kelly's opening brief. (pp. 72-77; 32-37).

**ANSWER TO THE SOUTHERN PACIFIC'S  
SPECIFICATION OF ERROR NO. 2, POINT FOUR  
SUMMARY OF ARGUMENT**

Although the judgment in *Powers v. Southern Pacific Company* is *res judicata* in this action, the damages there are not conclusive of the proper amount, if any, of damages to be recovered here.

**ARGUMENT**

The damages assessed in *Powers v. Southern Pacific Company* are not *res judicata* between the present parties although the verdict and judgment there are *res judicata* as to negligence. As has been shown, Booth-



Kelly contends the prior judgment shows the Southern Pacific Company to have been held in the first action solely for an independent act of its own negligence. The damages levied there are then *res judicata* as to the parties there, but are not *res judicata* against this defendant under the facts of this litigation. Therefore, the court below did not err when it refused to be bound by the amount of the prior judgment or the figure at which it was compromised.

In the first place, it is well established that:

“Issues not actually decided in the prior action are open.” (citing many cases) *Boston & M.R.R. v. T. Stuart & Son Co.*, 236 Mass. 98, 127 N.E. 532.

In certain cases, and this is one, the issue of damages is not decided insofar as the indemnitor is concerned.

Reporter headnote 3 of *Lord & Taylor v. Yale & Towne Mfg. Co.*, 230 N.Y. 132, 129 N.E. 346, states that if an indemnitee is obliged to defend the exclusive act of the indemnitor and the notified indemnitor fails to defend, the indemnitor is liable for the *damages* recovered *but*:

“the rule is otherwise where the the original defendant has to defend against *some negligence of its own*; hence, a master who was negligent in inspection cannot, by calling in the manufacturer of the appliance which broke, shift the entire burden of such manufacturer.” (emphasis supplied)



The annotation, 40 L.R.A. (N.S.) 1172, 1177, specifically covers the particular fact situation here:

“If the plaintiff in the action for indemnity was held liable in the original action on the ground of some negligence of his own, and if the extent of his liability was determined within certain limits by the degree of his own culpability or of that of the present defendants, then it cannot be held that necessarily, and as a matter of law, the defendants in the action for indemnity are liable to reimburse the plaintiff therein to the extent of the judgment recovered in the original suit, even if the present defendants have been properly notified to come and defend that suit.”

Authority for this assertion is found in *Consolidated Hand-Method Lasting Machine Co. v. Bradley*, 171 Mass. 127, 50 N.E. 464. (Pertinent quotation in Appendix I.) Since the damages were assessed with reference to the degree of culpability of the defendant therein, the amount of damages may be disputed when the first defendant sues for reimbursement. See also *Lowell v. Boston & Lowell Railroad Corp.* 23 Pick. (40 Mass.) 24, 35, cited by the Southern Pacific at page 21 of its brief.

Furthermore, it should be noted that the indemnity clause here does not in terms make any judgment rendered conclusive although the draftsman could easily have done so. Booth-Kelly merely agrees to indemnity

for "loss, damage, injury or death," not to accept the results of any litigation on such matters as conclusive of the proper amount of damages. In this aspect it is interesting to contrast the comparable clause in *Houston & T.C.R. Co. v. Diamond Press Brick Co.*, Tex. Civ. App., 188 S.W. 32. There the industry agreed to save the railroad harmless from any cause growing out of the operation of the spur track. Then the draftsman in a separate sentence provided that industry further agreed to reimburse the railroad for:

"\* \* \* any and all amounts it may be compelled to pay in settlement of any claim for which, under the terms of this agreement \* \* \*," (industry would be liable).

Here the omission of any words making the payment or compromise of a judgment conclusive is significant.

In summary neither by law in view of the facts of this case, nor by contractual agreement were the damages assessed in *Powers v. Southern Pacific Company* res judicata as to the defendant in this case. Yet the Southern Pacific in each one of its three Specifications of Error assumes that the California action is *res judicata* of the amount of damages to be recovered either by indemnity, contribution, or as liquidated damages for breach of contract.

**ANSWER TO THE SOUTHERN PACIFIC'S  
SPECIFICATION OF ERROR NO. 3  
SUMMARY OF ARGUMENT**

**POINT ONE:** The Southern Pacific seeks indemnity for the full amount of its loss plus its costs independently of the spur track agreement, but there is no other legal basis upon which a claim to indemnity can be based.

**POINT TWO:** Oregon authority, which is controlling, requires a contractual basis for recovery of indemnity; and the authorities cited by the Southern Pacific to sustain its claim for non-contractual indemnity all involve contracts.

**POINT THREE:** The rule of *Lowell v. Lowell* and *Boston Railroad Corp.*, as to contribution or indemnity, is repudiated in Oregon.

**POINT FOUR:** The only new point raised by this specification of error is whether an indemnity liability independent of the spur track contract exists here, and an analysis of the authorities shows that no indemnity liability exists here because there is no implied contract for indemnity.

**ARGUMENT**

Under this specification of error the Southern Pacific contends that it can recover the full amount of its loss and costs independent of contract. Such a recovery

would have to be based either on a right of indemnity or of contribution. Indemnity is based on contract express or implied. *Vandiver & Co. v. Pollak*, 107 Ala. 547, 552-553, 19 So. 180. For other authorities see 20 Words and Phrases, "Indemnity," "Contribution distinguished," 681 and 1950 Pocket Part 196.

Here the Southern Pacific does not seek proportional reimbursement so it seems clear that its claim is not for contribution. Furthermore, in Oregon no contribution exists between two persons who acting independently or jointly have injured a third person although one may have discharged their joint liability. *Fidelity & Cas. Co. of N.Y. v. Chapman*, 167 Or. 661, 120 P. 2d 223. And under this specification the Southern Pacific does not question the court's finding of fact that the Southern Pacific was guilty of some negligence. (T. 54). It is clear that the Southern Pacific cannot recover by the principle of contribution since that is rejected in Oregon when two persons acting independently or jointly negligently injure a third person.

The reliance of the Southern Pacific must then be on a right of indemnity, but indemnity springs from contract. Here recovery upon the express contract is disavowed. The only basis of indemnity remaining would then be an implied contract, yet a contract cannot be implied to cover the same subject matter which



the parties have expressly contracted about in minute detail. *Failing v. Osborne*, 3 Or. 498.

The Southern Pacific seeks to meet this lack of a contract by citing *Lowell v. Boston & Lowell Railroad Corp.*, 23 Pick. (40 Mass.) 24. In that case it is said that there was no contract, yet there are good grounds for believing an implied-in-fact contract existed there: the town by its inaction accepted the promise of the railroad's agent to keep up the barrier. *Scott v. Curtis*, 195 N.Y. 424, cited by Southern Pacific, also involves an implied contract of indemnity where the express contract to sell coal was silent on the point.

To summarize the only Oregon authority, *Astoria v. Astoria Col. R. R. Co.*, 67 Or. 538, 136 Pac. 645, cited for a non-contractual indemnity recovery involves an implied contract of indemnity. The fact that the Astoria case, *supra*, is distinguished in the Fidelity case, *supra*, upon the grounds that a contractual relationship existed is significant in view of Fidelity case's sweeping condemnation of the principle of contribution, a word which the Oregon court sometimes extends to include indemnity. (Astoria case, *supra*, 546-7.) The inference is clear: if there is to be indemnity, there must be a contract in Oregon. The court below agreed when it concluded that Booth-Kelly was not obliged to pay anything independently of the spur track agreement. (Conclusion of Law No. 6, 55.)



That is the clear implication of the Oregon court's analysis of the Astoria decision in the Fidelity case, *supra*, which is recent, being decided in 1941. The Astoria case, itself, is subsequent to the two non-Oregon authorities relied on. The Astoria case is fatal to the Southern Pacific's claim to indemnity on a non-contractual basis. Here there can be no implied contract of indemnity because well established contract principles prevent the implication of an implied contract of indemnity where an express contract exists.

The quotation from the Lowell case, *supra*, set out in the Southern Pacific's brief at page 22 is also quoted in the *Astoria v. Astoria River R. Co.*, 67 Or. 538, 547, 136 Pac. 645, but the Southern Pacific omits one sentence which is quoted in the Astoria case:

"In respect to offenses, in which is involved any moral delinquency or turpitude, all parties are deemed equally guilty, and courts will not inquire into their relative guilt." (P. 547)

This sentence is important because it tags Massachusetts as the jurisdiction the Oregon court had in mind in Fidelity & Cas. case, *supra*, when it said:

"In some jurisdictions where the offense is merely *malum prohibitum* and does not involve moral turpitude, it is not against the policy of the law to inquire into the relative delinquency of the parties and to administer justice between them although

both parties are wrongdoers. Contribution, however, in our opinion, practically means adoption of the doctrine of comparative negligence. Certainly the allowance of contribution between active tort-feasors on any basis of comparative negligence is contrary to the well-established rule in this state." (P. 665)

The court in the Fidelity & Cas. case, *supra*, goes on to distinguish the Astoria case making it doubly certain that the court had the Lowell case in mind when it denounced contribution.

Furthermore, in the Lowell case in the paragraph immediately preceding the quotation used in the Southern Pacific's brief, (P. 22), the words indemnity or contribution are used interchangeably. (Lowell case, *supra*, P. 32.) As has been pointed out, the Oregon court in the Astoria case, *supra*, where it quotes the Lowell case, also uses the terms indemnity and contribution interchangeably. (P. 546-7). So the inference is that when the court clearly repudiates the Lowell case, *supra*, as authority on contribution that the condemnation extends over to indemnity which both courts had previously used the terms interchangeably. In any case as a minimum the law represented by the quotation from the Lowell case, *supra*, has been repudiated by the Oregon Court in the Fidelity case, *supra*. (P. 665).

The Fidelity case, *supra*, is the clearest and most recent authority in Oregon on a non-contractual recovery.

It distinguishes the Astoria case, *supra*, on ground that there was a contract there. One is lacking under this specification of error.

The other authorities cited by Southern Pacific, if they are in point at all, go no further than also to assert that indemnity may be allowed the one secondarily negligent as against the one primarily negligent. (Lowell case, *supra*, 32; Scott case, *supra*, 428). But those authorities are not close enough on the facts to establish which party here was primarily negligent. Thus the question here becomes: who was primarily negligent?

It has already been argued at great length in this and the opening brief that the negligence of Booth-Kelly is here only secondary or passive. Those arguments are here relied on and hence not repeated. The only new point raised by this specification of error is not whose negligence was primary but is there any rule of law allowing a recovery here except by virtue of the spur track agreement. The controlling Oregon authority, the Astoria case, *supra*, requires at least an implied contract of indemnity for a recovery for indemnity. There can be no such recovery here because there is no implied contract on which the Southern Pacific can rely after having disavowed reliance on the express contract.

## **REPLY BRIEF OF APPELLANT BOOTH-KELLY LUMBER COMPANY**

(Appellant is referred to herein as "Booth-Kelly" and Appellee is referred to as "Southern Pacific" or "railroad.")

### **REPLY TO SOUTHERN PACIFIC'S ANSWER TO SPECIFICATION OF ERROR NO. 1 SUMMARY OF ARGUMENT**

The determinations in *Powers v. Southern Pacific Company* are *res judicata* against the Southern Pacific here. Therefore, although it is true that formally the rights between Booth-Kelly and the Southern Pacific were not litigated in the *Powers* case, certain issues were litigated which effectively determine in this action that the Southern Pacific is not entitled to indemnity under its contract.

### **ARGUMENT**

Although the question of the interparty rights between the Southern Pacific and Booth-Kelly are technically open in this action, the principles of *res judicata*, which bind both of the present parties, require conformance to the findings of the first action. An examination of the *Powers* case proceedings discloses that recovery was had there for certain failures of the Southern



Pacific which are not covered by its indemnity contract with Booth-Kelly. The question here is the applicability or non-applicability of the indemnity contract in the light of the facts found in the Powers case. Since the findings of the Powers case effectively prevent certain issues arising here, it was error for the court below to make Finding of Fact No. 18, and to enter Conclusion of Law No. 2. (T. 54, 55).

Conclusion of Law No. 2 states:

“2. The determinations in the Mack D. Powers’ action against plaintiff are not *res judicata* in this proceeding.”

The Southern Pacific fails to dispute Point Two under this specification of error, which contends that the determinations in the first action are *res judicata* against the notified indemnitor. Therefore, in effect it is conceded that so far as Booth-Kelly is concerned the determinations in the Powers case are *res judicata*.

As to Point One of this specification of error relating to the indemnitee railroad, the Southern Pacific agrees:

“\* \* \* so far as indemnitee is concerned the scope of estoppel created by the judgment in the primary case embraces all of the issues determined by it.” (Brief, 30).



Therefore, the inference is clear the Southern Pacific by its concessions, silent or express, agrees that the entry of Conclusion of Law No. 2 was erroneous.

That is sufficient to show that the court is in error, but despite these fatal concessions the Southern Pacific goes on to attempt to limit the authorities cited under Point One by Booth-Kelly by asserting that none of them go further than holding that the indemnitee cannot deny facts litigated in the first action. But this statement fails to make clear that those very facts may be a conclusive bar to the indemnitee's recovery. That is the significance of *Edinger & Co. v. S. W. Surety Ins. Co.*, 182 Ky. 340, 206 S. W. 465. (Booth-Kelly's Brief 12). The Southern Pacific attempts to distinguish this case by directing attention to irrelevant facts. The question here is the effect of the prior judgment on an indemnitee's claim against an indemnitor. The particular factual surroundings in which this principle is applied is here irrelevant, because the point is the scope of the controlling principle of law.

Part of the quotation made from the court's syllabus of *Central of Georgia Ry. Co. v. Macon Ry. & Light Co.*, 9 Ga. App. 628, 629, 71 S.E. 1076, shows how the generalization relied upon by the railroad must be understood:

"\* \* \* the plaintiff in the second action is estopped

from showing that the causes alleged in the prior action were not the true causes of the damages."

The railroad attempts to distinguish this case saying that no contract is involved. Here the question is what is the effect of the first judgment in the second action where a relationship of indemnity exists. The railroad now raises the irrelevant issue of how the relationship of indemnity arose.

The Southern Pacific makes the same fallacious distinction in respect to Comment (h) of Sec. 107, Restatement of the Law of Judgments, stating:

"\* \* \* the quotation cited was not meant to apply to a situation where a contract exists \* \* \*"

This criticism seems to be hardly in good faith when railroad fails to mention that in the next sentence following the section quoted gives as an illustration, the case of a car driver who sues his insurance company on his policy for indemnity. The railroad also suggests that the Restatement does not apply where the primary negligence of the indemnitor caused the accident. No authority is given for that assertion, and a reading of the quotation suggests no reason why that should be so. It is stated simply that if a finding in the prior action would discharge the indemnitor, the principle of res judicata would require his discharge in the second

action. Finally the matter of attorney fees is here governed by contract, and the contract as drawn failed to provide for such.

The Southern Pacific analyzes *Hudson Valley Railway Co. v. Mechanicville E. L. & C. Co.*, 101 Misc. Rep. 152, 166 N. Y. S. 816, *reversed on other grounds*, 180 App. Div. 86, 167 N. Y. S. 428, and contends that it supports the Southern Pacific. The Southern Pacific's analysis relies on the opinion on appeal where the lower court's finding that the parties were in *pari delicto* was reversed. But the reason for citing the Hudson Valley case here is its ruling as to the conclusiveness of the original judgment in the second action as to the ground of liability in the first action. That authority is not questioned by the reversal on the contribution point.

Any possible conflict of the two Hudson Valley opinions as to the point now in question is resolved by the decision of the Court of Appeals in *Fulton County Gas & Electric Co. v. Hudson River Telephone Co.*, 200 N. Y. 287, 93 N. E. 1052, which is relied on in both opinions in the Hudson Valley case. (A lengthy quotation therefrom is set out in Appendix II.)

The quotation makes clear what was presented summarily in the Hudson Valley case; namely, the indemnitee is concluded as to the ground of its liability found by the verdict in the first action. The principle of res

judicata prevents assertion that the recovery was not based on the earlier ground. This earlier ground then in turn may be a fact fatal to the indemnitee's recovery over as it was here.

The railroad relies on *Astoria v. Astoria & Columbia River R. Co.*, 67 Or. 538, 136 Pac. 645, as a case analogous on the facts. Although the case is in point in certain respects, the examination of the *Astoria* complaint is not particularly helpful here in determining what party was primarily negligent. The reason it is not helpful here is that the facts are different. In the *Astoria* case a pedestrian was injured by a fall from a ramp leading to a track located in a public street.

**REPLY TO SOUTHERN PACIFIC'S  
ANSWER TO SPECIFICATION OF ERROR NO. II  
SUMMARY OF ARGUMENT**

The fact that Powers recovered against the Southern Pacific only on the ground that the Southern Pacific failed to provide him with a safe place to work, is a fact fatal to Southern Pacific's recovery here. The determinations in the Powers action are controlling here because in this case they prevent the indemnity contract coming into operation. Booth-Kelly was not responsible for the Southern Pacific's failure to pro-



vide a safe place to work and could not be since the duty is non-delegable.

### ARGUMENT

The Southern Pacific in its claim that the Powers case established only that the Southern Pacific failed to provide its employee with a safe place to work fails to note or to meet that the fact of Powers' recovery on that basis there is a fact fatal to its own recovery here. The railroad goes on to assert that Booth-Kelly was responsible for Southern Pacific's failure to provide a safe place to work. No finding of the court below to that effect is cited. Furthermore, to so argue is to ignore the undisputed fact that under the Federal law the duty to provide a safe place to work is non-delegable.

Booth-Kelly agrees that in a sense the ultimate responsibility as between the parties for the accident was not determined in the Powers case. This action, therefore, became necessary; but Booth-Kelly does assert and it is the crux of the matter that the facts litigated and determined in that case show that Southern Pacific is barred here. The Southern Pacific is barred here because the facts there determined show as a matter of law that the Southern Pacific was held for its *own act alone*—something which the indemnity contract does not cover. Since the previous adjudged facts show, as a matter of law, the cause of the loss, it was error for the



court below to redetermine the proximate cause, as it did in Finding of Fact No. 10. The fact that this wrongful redetermination resulted adversely to Booth-Kelly is the basis for asserting that error is prejudicial.

Actually, Booth-Kelly does not need to assert that the Southern Pacific's negligence was the sole negligence in that case. (Although it does so assert.) It is enough for it to assert that the recovery against the railroad was for the acts of the railroad alone. Since the recovery was for the acts of the railroad alone, neither of the indemnity categories were met. The Southern Pacific was not held in the Powers case for an act or omission of Booth-Kelly. The Southern Pacific was not held in the Powers case for the joint negligence of both parties. The Southern Pacific was held in the Powers case for its own act, a failure to provide its employee with a safe place to work.

The contention that Booth-Kelly might have been sued successfully by Powers, even if true, is immaterial here. In that case Powers would have had to recover from some negligence of Booth-Kelly. Here the Southern Pacific seeks indemnity for its own negligence.

Attempt is made by counsel to distinguish the authorities cited for the proposition that failure to warn is an independent act of negligence. The gist of the distinctions drawn is that in each of those cases the jury

found in the first action that the city (indemnatee) was guilty of some independent act of negligence, not covered by the contractor's bond. But that is one of the very reasons the cases were cited; here, too, the railroad was found guilty of an independent act of negligence which the indemnity contract (like the contractor's bonds) does not cover.

*U. S. Fid. & Guar. Co. v. Thomlinson*, 172 Or. 307, 324, 141 P. 2d 817, was cited to show the correct rule of construction where the indemnatee was solely negligent. Here examination of the proceedings in the Powers case show that the railroad was held for an act which it could alone have failed to do, failure to provide a safe place to work, so the case cited is in point.

Point Two of this Specification of Error points out that the court below erred when it found that certain alleged negligence of Booth-Kelly was the proximate cause of Powers' injury (Finding No. 10, T. 53). Such a finding was error as a matter of law, as certain closely analogous spur track cases show. (Opening brief: 32-34.) The Southern Pacific seeks to distinguish these cases; that the distinctions are fallacious has been pointed out in detail above. (pp. 23-6). The only Oregon authority suggested as in point is the *Astoria v. Astoria & Columbia River R. Co.*, 67 Or. 538, 136 Pac. 645, which is not close enough on the facts to be helpful in determining whose

negligence here was the proximate cause of negligence. Finally, the Southern Pacific makes no effort to avoid the effect of *Keller v. City of Fargo*, 49 N.D. 562, 192 N.W. 313, which shows by analogy that the judgment in the first action necessarily determines the negligence of the indemnitee was the proximate cause of the injury. (Brief 35-37). The issue of proximate cause was therefore res judicata, and the court below erred in making Finding of Fact No. 10 as a matter of law.

**REPLY TO SOUTHERN PACIFIC'S  
ANSWER TO SPECIFICATION OF ERROR NO. III  
SUMMARY OF ARGUMENT**

Since Oregon statutes compel the construction of and operation on spur tracks by the railroad, the spur track agreement, specifically the indemnity section thereof, was without consideration as to Booth-Kelly since the railroad was obliged to serve Booth-Kelly as a matter of law and therefore could not impose conditions by contract.

**ARGUMENT**

The fact that the application of the Federal Employers' Liability Act to Powers' claim may establish that interstate commerce was involved, but there is no warrant for saying that *therefore* the requirements of

Federal law with regard to operations on private industrial spur tracks are applicable. Here the Southern Pacific is suing on a contract of indemnity. The question is consideration for that contract. That in turn becomes a question of what law controlled the negotiation of that contract.

Here the Federal government by statute has in effect delegated certain powers to the states. 49 U.S.C.A. sec. 1 (22) (set out at p. 38 of opening brief). Oregon has filled that gap by exercising its delegated powers, and as has been argued in detail in the opening brief, those Oregon statutes compel spur track service of the sort provided by the contract. (Brief 38-51). Therefore, the contract lacks consideration. On this the Oregon law controls, and it controls because the federal government has specifically left this matter to the states.

As has been pointed out earlier in this brief at pages 4-5, 49 U.S.C.A. sec. 1 (9), is not in point here because 49 U.S.C.A. sec. 1 (22) is controlling. Briefly, the distinction is that Section 1 (9) deals with a switch connection to existing track or track which may be required to be preexisting; Section 1 (22) deals with the construction of spur tracks wholly within one state.

The Southern Pacific relies strongly on *Luton Mining Co. v. Louisville & N. R. Co.*, 276 Ky. 321, 123 S. W. 2d 1055, which is not in point. Attention is directed to



a quotation made from that case by the Southern Pacific:

“It is not required by law to perform the service. The *only* obligations imposed on it were by virtue of paragraph 9 of Section 1 of the Interstate Commerce Act, as amended, 49 U.S.C.A., sec. 1 (9) \* \* \*” (Emphasis supplied.) (Brief 38).

It is evident that the Luton case, *supra*, is not in point here since there Section 1 (9) was deemed controlling. There the question was a switch connection; here it is a spur track wholly in one state. It is significant that the court distinguishes *Cleveland C.C. & St. L.R.R. v. U.S.*, 272 U.S. 404, 48 S. Ct. 189, 72 L. Ed. 338, which case as has been pointed out involved the application of Section 1 (22). It was therefore correct for the court in the Luton case, *supra*, to say that the only obligation imposed by law was by Section 1 (9) which leaves no room for the application of state law. Here Section 1 (22) is controlling, and under it the Oregon statutes impose an obligation.

The Luton case, *supra*, states that in that case there was consideration on account of the construction of the track. It relies on the case of *Gorman Coal Co. v. Louisville & N.R. Co.*, 213 Ky. 551, 281 S.W. 487, but in that case there were no Kentucky statutes compelling the construction of spur tracks as there are in Oregon. Sec-



ondly, the placing and removal of cars on such tracks is not consideration here because such service is also compelled by the Oregon statutes. These statutes are set out in the opening brief: 8 O.C.L.A. 113-108 and 109. (Brief 40-41) In addition 8 O.C.L.A. 113-129 (c) required the railroad to furnish cars. (Text in Appendix III) (Finally 8 O.C.L.A. 113-108, although similar to 49 U.S.C.A. 1 (9), is not identical on the important provisions here.)

No authority is cited for limiting 8 O.C.L.A. 113-104 to spurs on the railroad's own premises available to all shippers except *Southern Pacific Co. v. Railroad Com.*, 60 Or. 400, 119 Pac. 727. Nothing in that case so asserts and it does not appear that the spur there was to be put on the railroad's own premises. Also to be considered against this restrictive interpretation is the fact that railroads have the power of eminent domain to provide spur tracks necessary. (Railroad Com., *supra*, 414.) Finally, the tracks here were at least partly on property owned by the railroad, and the railroad served other shippers on the same spur as well as using the track for general switching purposes. (T. 89, 104, 105; see blueprint attached to Ex. 1.)

8 O.C.L.A. 113-109 is in point here. That section refers simply to a warehouse not to a public warehouse. As *State v. Wilson*, 47 N.H. 101, 106, shows the term is

broad enough to cover any building where a manufacturer's products such as cut lumber is stored awaiting shipment. (Quotation in Appendix IV) Second, an inspection of the scale drawing blue-print attached to Exhibit 1, will show that the Booth-Kelly mill buildings were less than 150 feet from the main line of the railroad.

**REPLY TO THE SOUTHERN PACIFIC'S  
ANSWER TO SPECIFICATION OF ERROR NO. IV  
SUMMARY OF ARGUMENT**

The first sentence of Section 7 should be construed to modify the second and only other sentence since both sentences deal with indemnity. Since recovery was allowed on the contract in the court below, the question of the construction of that contract is material here, and the question was properly specified as error since it was specified that the court erred in allowing a recovery on the contract.

**ARGUMENT**

Testimony that the Southern Pacific was returning from delivering logs to Springfield Plywood Company at the time of the accident was uncontradicted. (T. 90). The court is asked to construe the contract here and ascertain if such a situation is covered by serving industry clause. That legal question of construction is open

because it has been specified as error that the court below allowed recovery *on the contract*. (Brief 53). The construction argued here and presented to the court below and inferentially rejected would bar recovery on the contract. (T. 112).

Counsel attempts to distort the question of serving industry into whether Booth-Kelly benefited from those operations. That is obviously a different question; here the question is the construction of the contract, and words are: "serving said Industry." The contract states that "Industry" is the Booth-Kelly Lumber Company. (T. 5). Service to the plywood company was not service to Booth-Kelly.

Even if it were a question of benefit there is no showing here that Booth-Kelly benefited. The following facts are to the contrary, and tend to show that the railroad benefited. An inspection of the blue-print attached to Exhibit 1 shows that the great bulk of the track was owned by the railroad. There was uncontradicted testimony that the Huntington Shingle Mill, one of the industries on the track, was located partly on Southern Pacific property. (T. 105). The fact other unloading facilities do not show upon the blue-print attached to Exhibit 1 is immaterial in view of the fact this particular contract concerned only Booth-Kelly and it would be expected that only Booth-Kelly's facilities

would be shown. Furthermore, it was specifically provided that the railroad might use the track to serve others than Booth-Kelly. (T. 8).

**REPLY TO THE SOUTHERN PACIFIC'S ANSWER TO  
SPECIFICATION OF ERROR NO. V  
SUMMARY OF ARGUMENT**

The Oregon law as stated in *Southern Pacific Company v. Layman* is controlling, and it provides that an agreement to indemnify an indemnitee against its own negligence is void as contrary to public policy. The court below applied the concurring negligence clause, but this clause is void as contrary to the public policy stated. Even the general law would not consider the concurring negligence clause valid in view of the facts of this case.

**ARGUMENT**

As between the concurring negligence and the act or omission clauses, only the concurring negligence clause would allow indemnity to the railroad for its own negligence. The concurring negligence clause which splits any liability was in fact applied. This is conveniently summarized by the court in its decision:

“However, since the railroad was in some measure also at fault which contributed to the accident, judgment is given under the contract for only one-half of the damage.” (T. 117).



Although as appellee the railroad is presumably trying to uphold the judgment below, its argument here is based on the act or omission clause which the court did not apply.

Since the concurring negligence clause which was applied allows the railroad to be indemnified for its own negligence, it was error for the court below to apply that clause here since it was void under the Oregon law as stated in the Layman dicta. Under this specification of error, the Layman case, *supra*, has no other pertinence because it deals with the problem of the construction of an indemnity agreement. This dicta must prevail over any earlier dicta in *U.S.F. & G. Co. v. Thomlinson Co.*, 172 Or. 307, 325, 141 P. 2d 817, cited by the railroad, especially since the Layman dicta is a considered recognition of the weight of authority supported by citations while the Thomlinson dicta is a hypothetical aside in a discourse.

Although Oregon authority is controlling, the railroad relies on non-Oregon cases to support the validity of the contract here (Brief 47). None of those cases is in point here because they do not involve the construction of a concurring negligence clause as distinct from a blanket indemnity clause, and in only one of them is there a concurring clause like the one here. Finally none of the authorities relied on go further than to



state that a railroad may make such indemnity contracts when acting in a private capacity. They do not contradict the rule laid down by the United States Supreme Court:

“It is the established doctrine of this court that common carriers can not secure immunity from liability for their negligence by any sort of stipulation. (citations)” *Railway Co. v. Grant Bros.*, 228 U.S. 177, 184, 33 S. Ct. 474, 57 L. Ed. 787.

Thus it is clear that if the Southern Pacific was acting in its capacity of common carrier it could not contract away its liability for negligence. Here the railroad was acting as a common carrier when it provided spur track service pursuant to 8 O.C.L.A. 113-104, 113-108, 113-109, 110 (The texts of the statutes and their general applicability are set out in the opening brief at pages 40-42 and 47-51).

Even if it was acting in its private capacity, there are certain exceptions to the rule that such indemnity contracts may be made which void the contract here. First, the rule does not extend to cases where the spur is used for purposes disconnected with the business of the industry. *William Danzer & Co. v. Western Md. Ry. Co.*, 164 Md. 448, 165 A. 463. There the sidings were being used as a storage and switching yard in a way which was disconnected with the business of the industrial plant. Here

the siding was also used for general switching purposes and to serve other industries. (T. 89, 105).

Second, the rule does not apply where the siding is located on the property of the railroad even though it was constructed at the request and for the benefit of a shipper who also paid part of the cost of construction. *Stoneboro & C. L. Ice Co. v. Lake Shore & M. S. R. Co.*, 238 Pa. 289, 86 A. 87. Here at least part of the track was located on land owned by the railroad. (T. 104; also see blue-print attached to Ex. 1.)

Counsel's attempt to distinguish the cases cited by Booth-Kelly at page 68 of its brief is faulty in two ways. First at least two of the cases do not involve public service companies or relationships: *Nashua Paper Co. v. Noyes Buick Co.*, 93 N.H. 348, 41 A. 2d 920; *Jankele v. Texas Co.*, 88 Utah 325, 329, 54 P. 2d 425. Second, the services rendered by the Southern Pacific did not extend beyond those required by law as has already been pointed out.

### **REPLY TO THE SOUTHERN PACIFIC'S ANSWER TO SPECIFICATION OF ERROR NO. VI**

The question here is not responsibility or the indemnity clauses but the step before that: causation attributable to any alleged breach. That was analyzed in the opening brief by the use of closely analogous cases on

the facts (pp. 72-76); counsel is content to rely on assertions as to cause unsupported by authority. Counsel's sole resource is an attempt to distinguish Booth-Kelly's spur track cases, but as has been shown earlier in this brief, the distinctions drawn are fallacious. (pp. 23-6). It is to be noted that the railroad makes no effort to meet the contentions of Booth-Kelly that the movement of cars here was negligent and to switch on an obstructed track is itself negligent as a matter of law. (Brief 73-76). Finally, in addition to the testimony of Witness Nysten (T. 99-102), Exhibit 15, railroad rules as to maintenance of way, shows the existence of the custom as to removal of obstructions and constitutes adequate proof of the custom. (Rule No. 1094; set out at p. 75 of opening brief.)

### CONCLUSION

In conclusion, it is submitted for the reasons and authorities cited in this and the opening brief the cross-appeal should be dismissed and the judgment below reversed.

Respectfully submitted,

VEAZIE, POWERS & VEAZIE  
and JAMES ARTHUR POWERS

# I

## APPENDIX I

In *Consolidated Hand-Method Lasting Machine Co. v. Bradly*, 171 Mass. 127, 50 N.E. 464, the court says at page 133:

“We are also of opinion that the original action was such that by any form of notice the present defendants could not necessarily, as matter of law, be held bound by the judgment in that action. The damages in that action were assessed with reference to the degree of culpability of the defendant therein, or of some person for whose negligence the defendant was made liable by St. 1887, c. 270. The defendants in the present suit, if they are liable at all to the plaintiff, are liable at common law for breach of their contract or of their duty. The defendant in the original action was defending against its own negligence or the negligence of persons for whom it was responsible.”

## APPENDIX II

In *Fulton County Gas & Electric Co. v. Hudson River Telephone Co.*, 200 N.Y. 287, 93 N.E. 1052, the court states at page 1055:

“The plaintiff must in this action accept the transaction in its entirety. The facts upon which the judgment in the Horning action was recovered are an essential and ineradicable part thereof, which the plaintiff may not deny, contradict, abandon, or supplant with other facts \* \* \* If this defendant is by that judgment concluded on the question of Horning’s damages and this plaintiff’s liability, this plaintiff is concluded thereby as to the ground of its lia-

## II

bility as found by the verdict of the jury and is not permitted to free itself from such verdict and the ground thereof, or reopen the issues litigated and adjudicated in the action in which the judgment was rendered. \* \* \*

“Therefore, if it appears that the judgment in the Horning action was based upon a finding of fact fatal to recovery in this action, it cannot be maintained. The judgment in the Horning action is conclusive proof that the plaintiff in this action was legally liable to Horning upon the ground adjudicated in that action, if a ground were adjudicated, in the amount of the verdict therein. The record therein may disclose a state of facts showing that the defendant is or is not liable over to the plaintiff.”

## APPENDIX III

8 O.C.L.A. section 113-129(c) provides in part:

“(Failure to furnish cars: Demurrage and damages.) Any railroad neglecting or refusing suitable cars when applied for in conformity with the orders, rules and regulations prescribed by the commission (commissioner), and within the time therein stated, shall be held to be immediately indebted and liable to pay to such applicant a sum per day equal to the demurrage per diem charge which the commission (commissioner) may, by its order, have determined, \* \* \* and in addition thereto all damages actually sustained by reason of the said car or cars not being so furnished.”



### III

#### APPENDIX IV

The court in *State v. Wilson*, 47 N.H. 101, 106, defines warehouse as follows:

“A warehouse in the more limited sense is the building or place in which a warehouseman deposits the goods of others in the course of his business; and this limited construction was given to the word in *Owen v. Boyle*, 22 Me. 47. But in common discourse I understand the word is applied to buildings used for the temporary storage of merchandise before it is put into market for sale, or put in the course of transportation by sea or land to another place, though the buildings may not belong to a warehouseman but to the owners of the goods: such are the buildings in which manufacturers keep their goods for a time before they put them into market for sale or send them abroad it would seem to be the opinion of Bishop as cited by counsel, that the common and legal understanding of the term is the same; that in legal construction as well as in the common understanding of the word it would extend so as to include buildings of individuals or corporations where they store their own goods temporarily in distinction from the places where they are offered for sale or kept by the owners permanently till they are needed for use.”



# In the United States Court of Appeals

For the Ninth Circuit

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Appellee,*

AND

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Cross-Appellant,*

vs.

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Cross-Appellee.*

---

**Appeal and Cross-Appeal from the United States District Court  
for the District of Oregon**

HONORABLE JAMES ALGER FEE, *Judge*

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## REPLY BRIEF OF CROSS-APPELLANT

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KOERNER, YOUNG, SWETT & McCOLLOCH,  
JAMES C. DEZENDORF,  
ALFRED H. CORBETT,

800 Pacific Building, Portland, Oregon,  
*Attorneys for Cross-Appellant and Appellee*

VEAZIE, POWERS & VEAZIE, and  
JAMES ARTHUR POWERS,

611 Corbett Building, Portland, Oregon,  
*Attorneys for Cross-Appellee and Appellant.*

**FILED**

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No. 12340

# In the United States Court of Appeals

For the Ninth Circuit

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Appellee,*

AND

SOUTHERN PACIFIC COMPANY, a Corporation,  
*Cross-Appellant,*

vs.

BOOTH-KELLY LUMBER COMPANY, a Corporation,  
*Cross-Appellee.*

---

**Appeal and Cross-Appeal from the United States District Court  
for the District of Oregon**

**HONORABLE JAMES ALGER FEE, *Judge***

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**REPLY BRIEF OF CROSS-APPELLANT**

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## **PRELIMINARY STATEMENT**

(Cross-Appellant is referred to herein as "Southern Pacific" or "Railroad" and Cross-Appellee is referred to as "Booth-Kelly" or "Industry".)

This is a case arising out of an industrial spur track agreement, which was occasioned by Southern Pacific's being requested to undertake services not required of it

by statute and to thereby run the risk of liability which it could not have been forced to assume by law. The Railroad was asked to run across property "used or owned by defendant" (T. 51), in other words, to run through property the control of which was in Booth-Kelly's hands. Under these circumstances it was reasonable that Southern Pacific should exact as the quid pro quo for its undertaking, that Booth-Kelly would respect the specified clearance distances and would save Southern Pacific harmless from any liability arising out of some act of Booth-Kelly on that land or caused by the omission by Booth-Kelly of its duties in connection with the premises over which Southern Pacific was to operate.

Booth-Kelly breached that agreement by placing the cart dangerously close to the track and by omitting to remove it, although trains were operating over the track. The accident arose out of the placement of an obstruction in violation of specific agreement, which obstruction was under the control of Booth-Kelly. As a result, Southern Pacific has been obliged to pay damages to its employee Powers.

What is concerned in this appeal is the responsibility for the accident as between Southern Pacific and Booth-Kelly under the provisions of the industrial track agreement. This fundamental point is often overlooked in Booth-Kelly's answering brief, where in many instances cases are used and arguments made as if no agreement were in existence. The question of ultimate responsibility as between the parties may be entirely altered by con-

tract. Since a contract exists in the present case, its provisions must be laid over the factual base to bring out the ultimate pattern of responsibility.

## SPECIFICATION OF ERROR NO. 1 BREACH OF CONTRACT

### Summary of Argument

**Booth-Kelly cannot escape liability for damages for breach of contract by setting up the determination in the Powers case, since recovery in that action was the natural and necessary result of the breach of contract.**

Booth-Kelly's promise to observe the minima prescribed clearances was one of the bargained for considerations given in exchange for Southern Pacific's agreement to operate over the industrial spur track, crossing land owned or used by Booth-Kelly.

Southern Pacific's agreement to give service on that track was valid consideration for Booth-Kelly's promises since the railroad was not obligated by law to go beyond the switch connection on its own right of way. (S. P. Brief pp. 34-40).

49 U.S.C.A. Sec. 1 (9),  
*Luton Mining Co. v. Louisville & N. R. Co.*, 276  
Ky. 321, 123 S. W. (2d) 1055.

No issue was raised in the trial court concerning the private nature of the track (Finding of Fact No. 2, T. 51), hence Section 1 (22) of 49 U.S.C.A. has no application. It applies only to tracks built and operated by a railroad as a part of its own system, not to private tracks operated under agreement.

The loaded wood cart constituted "material" and an "obstruction" which was "stored or maintained" in violation of the provisions of Section 5 of the agreement. (S. P. Brief p. 49). The cart hurt Powers. It was placed and maintained in position by Booth-Kelly. The location selected for the cart violated the minima for clearances in the agreement. The causal chain between the injury and the defendant is unbroken. The initial placing was wrongful. The lapse of time could not minimize the breach.

Southern Pacific was entitled in undertaking to serve over Booth-Kelly's spur track to protect itself against the risks to which it exposed itself. 9 *Am. Jur. Carriers*, Sec. 737. It could reasonably assume that accidents would occur if clearance lines were violated. The trial court correctly found that the damage to Powers and the liability of Southern Pacific was the natural and necessary result of Booth-Kelly's breach of contract in violating those clearances. (Finding of Fact No. 13, T. 53-4).

Southern Pacific is entitled to recover the amount of damages obtained from it by its employee, and the costs of defending the action, since such recovery and costs were reasonably within contemplation of the parties at the time of making the contract.

Booth-Kelly cannot by technical arguments avoid the consequences of its breach of contract.

Neither waiver nor estoppel is applicable to this case (S.P. Brief pp. 50-51).

The provision permitting Southern Pacific to cease operations over the track was for the railroad's protec-



tion. Booth-Kelly cannot make use of that provision to avoid the consequences of its own wrongful act. It could have removed the cart at any time and thus cured its breach and avoided liability.

Although the trial court concluded that the matter of control over the spur track had no material bearing on the determination of the case (Conclusion of Law No. 4, T. 55) Booth-Kelly seeks at inconsistent intervals to make much of the point. (B.-K. Answer Brief pp. 8, 13). Counsel apparently forgets his reference on page 25 of Booth-Kelly's opening brief to the California court's determination that Southern Pacific had no right to remove the cart.

## SPECIFICATION OF ERROR NO. 2 ENFORCEMENT OF INDEMNITY PROVISIONS POINT ONE

### Summary of Argument

**The Powers action established only that Southern Pacific failed to provide its employee with a safe place in which to work and did not determine the ultimate responsibility as between the parties to this action. Booth-Kelly was responsible under the agreement for Southern Pacific's failure to provide a safe place to work.**

In this action, where recovery is sought under an indemnity provision in a contract, the action must of necessity be predicated on loss or damage first suffered by Southern Pacific. That loss was suffered by reason of Powers' recovery in the California action. The parties are here litigating the question of ultimate responsibility for that loss.

The Powers case was concerned only with a determination of Southern Pacific's responsibility to its employee under the Federal Employers Liability Act, and with the amount of damage suffered by Powers. It was determined there that Southern Pacific had breached its statutory duty of providing its employee with a safe place within which to work.

No question of relative responsibility as between Southern Pacific and Booth-Kelly was there determined since Booth-Kelly was not a party to that action. Hence there could not have been a determination, contrary to Booth-Kelly's argument, that Southern Pacific was *solely* responsible for the accident.

Neither was there discussion nor application of the spur track agreement, since that issue was not material to the trial of Powers' claim. The application of the agreement to the facts was left for determination in this action between the parties to the contract.

The Powers case did establish Booth-Kelly's responsibility for the presence of the cart. It is an admitted fact and it was found by the trial court that the wood-cart was the property of Booth-Kelly and had been placed or left by it or its employees alongside the track on premises owned or used by Booth-Kelly (T. 34, 52).

Since the findings of the trial court that Booth-Kelly's negligence constituted the primary cause of the injury to Powers are consistent with the facts and are not in conflict with the determinations in the Powers case, no error

was committed in entering Findings of Fact 9 and 10. *Fed. Rules of Civ. Proc.* 52 (a).

Booth-Kelly has not been successful in distinguishing the Oregon cases cited in Southern Pacific's opening brief.

In *Astoria v. Astoria & Columbia River R. Co.*, 67 Or. 538, 136 Pac. 645, although the city could not by contract prevent recovery for the city's failure to care for the safety of the travelling public, it was able by contract to shift the ultimate responsibility for Mrs. Anderson's injuries to the railroad. Here, while Southern Pacific could not by contract prevent recovery against it for failing to provide a safe place within which to work, it did by contract place upon Booth-Kelly the ultimate responsibility for Powers' injuries. There the city was held liable by reason of its failure to enforce an ordinance. Here Southern Pacific was held liable for failing to enforce a contract requiring Booth-Kelly to observe clearance lines.

Since no determination was made either in the Powers case or by the trial court that Southern Pacific was *solely* negligent, but on the contrary it was found that Booth-Kelly was negligent and its negligence was the "active, direct, proximate and primary cause" of the injury to Powers, the attempt to minimize the dictum from *Southern Pacific Company v. Layman*, 173 Or. 273, 145 P. (2d) 295, likewise fails. (S. P. Brief p. 16).

The *Layman* case arose on demurrer to plaintiff's allegations that the indemnitee railroad suffered loss *solely* by reason of its own negligence, a situation which does not apply here. As stated in Southern Pacific's

opening brief at page 16, the Oregon court indicated that in a case where the contract created a duty in the indemnitor, "his negligent failure to discharge that obligation might be the primary cause of an accident \* \* \* which would result in injury to passengers and a consequent liability to the defendant (railroad)." In such a case, the indemnity provision might be evoked.

Thus the trial court's finding of primary responsibility against Booth-Kelly is supported by Oregon law, and should not be disturbed.

Although counsel cites cases from other jurisdictions, they cannot of course take the place of Oregon law. Furthermore it is impossible to divorce, as counsel attempts, the question of ultimate responsibility from the agreement entered into between the parties. While the cases involving liability to third persons or employees might be determinative of an appeal in the Powers case, they are not helpful in deciding the responsibility as between Booth-Kelly and Southern Pacific under the agreement.

## POINT TWO

### Summary of Argument

**It was error for the trial court to make a finding of concurrent negligence on grounds not made an issue in the Pre-trial Order.**

Although the Pre-trial Order contained detailed charges of negligence against Southern Pacific (T. 36-44) the trial court found that Southern Pacific was not negli-

gent in the form of the specifications there set out. Since the injury to Powers was not caused by any negligent act as charged in the Pre-trial Order, and was not caused by the continuing of operations after Southern Pacific's employees observed the position of the cart, we fail to ascertain any evidence in the record supporting the Court's 14th Finding of Fact.

### POINT THREE

#### Summary of Argument

**The application of the joint or concurring negligence clause of the indemnity provision is limited to situations where Booth-Kelly's duty was not fixed by contract.**

Under the industry track agreement Booth-Kelly was obligated to observe clearance minima. This it did not do, and its negligent failure in this regard and specific breach of its contractual duty was the primary cause of the injury to Powers. To limit recovery against Booth-Kelly to one-half in such situations would ignore the contract provision placing on Booth-Kelly the duty to maintain clearance distances free from obstructions. Such a holding would be inconsistent with the intent of the parties.

*Salt River Valley Water User's Ass'n. v. Cornum*, 49 Ariz. 1, 63 P. (2d) 639, is not in point since no agreement was involved.

Far from holding Southern Pacific solely negligent, the instant case establishes Booth-Kelly responsible for the injury to Powers. (Finding of Fact No. 10, T. 53).



Hence the discussion in *Deep Vein Coal Co. v. Chicago E. I. R. Co.*, 71 F. (2d) 963, is in point. (S. P. Brief p. 18).

## POINT FOUR

### Summary of Argument

**Booth-Kelly is bound by all matters determined in the Powers case. The amount of damages there determined were in excess of the \$44,699.46 settlement.**

Under authority of *Astoria v. Astoria & Columbia River R. Co.*, 67 Or. 538, 136 Pac. 645, Booth-Kelly is bound by the determination in the California action that Powers suffered injuries in the sum of \$46,100.00. Booth-Kelly is not hurt by the settlement for a lesser amount. (See P. T. Order VI, T. 35).

Counsel's attempt to distinguish the *Astoria* case is not persuasive. Depending upon the point involved, Booth-Kelly has argued (1) the judgment in the prior action is conclusive of the facts thereby established (B.-K. Opening Brief p. 16), (2) the damages are not *res judicata* although the verdict and judgment are *res judicata* as to negligence. (B.-K. Answer Brief p. 35).

## SPECIFICATION OF ERROR NO. 3

### Summary of Argument

**Recovery is permitted independent of contract where one tort-feasor is primarily negligent and the other secondarily so.**

Under this point we have cited authorities showing the extent to which the Oregon court, and courts in other jurisdictions have gone in allowing recovery to one held liable for tort, independent of any contractual right.

*Astoria v. Astoria & Columbia River R. Co.*, 67 Ore. 538, 136 Pac. 645, cites with approval *Lowell v. Boston & Lowell R. Corp.*, 23 Pick. 24. In *Fidelity & Cas. Co. of N. Y. v. Chapman*, 167 Or. 661, 120 P. (2d) 223, the court takes pains to point out that action it was deciding was “\* \* \* not a case where one tort-feasor is primarily negligent and the other secondarily so.” By so doing it left the door open for contribution in such cases.

See also *Hudson Valley Ry. Co. v. Mechanicville E. L. & G. Co.*, 180 App. Div. 86, 167 N.Y.S. 428, commented on in Southern Pacific’s answer brief p. 27.

### CONCLUSION

The question here involved is the ultimate responsibility under the spur track agreement for the injury to Powers and resultant liability of Southern Pacific. Under the agreement Booth-Kelly was primarily responsible for maintaining the clearance lines free from obstruction. Since the placing of the cart was not only in violation of

contract but was the primary cause of the injury to Powers, Southern Pacific is entitled to recover under the contract the full amount of \$44,699.46 judgment costs and \$1869.53 costs and attorneys' fees. Insofar as it fails to award these amounts the judgment appealed from should be modified.

Respectfully submitted,

KOERNER, YOUNG, SWETT & MCCOLLOCH,

JAMES C. DEZENDORF,

ALFRED H. CORBETT,

*Attorneys for Cross-Appellant.*

No. 12341

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**In the United States Court of Appeals  
for the Ninth Circuit**

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**JACOB CORNET, APPELLANT**

*v.*

**TIGHE E. WOODS, HOUSING EXPEDITER, OFFICE OF THE  
HOUSING EXPEDITER, APPELLEE**

---

**APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE  
NORTHERN DISTRICT OF CALIFORNIA, SOUTHERN DIVISION**

---

**APPELLEE'S BRIEF**

---

**ED DUPREE,**

*General Counsel,*

**A. M. EDWARDS, Jr.,**

*Acting Assistant General Counsel,*

**FRANCIS X. RILEY,**

*Special Litigation Attorney,*

*Office of the Housing Expediter, Washington 25, D. C.*

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**FILED**

**FEB 12 1950**

**PAUL P. O'BRIEN,**

**CLERK**





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# **In the United States Court of Appeals for the Ninth Circuit**

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No. 12341

JACOB CORNET, APPELLANT

*v.*

TIGHE E. WOODS, HOUSING EXPEDITER, OFFICE OF THE  
HOUSING EXPEDITER, APPELLEE

---

*APPEAL FROM THE UNITED STATES DISTRICT COURT FOR  
THE NORTHERN DISTRICT OF CALIFORNIA, SOUTHERN  
DIVISION*

---

## **APPELLEE'S BRIEF**

---

### **COUNTERSTATEMENT OF THE CASE**

This is an appeal by the defendant in the Court below from a judgment of restitution for overcharges of rent, contrary to Section 206 (a) of the Housing and Rent Act of 1947 (50 U. S. C. A. 1881, et seq.),<sup>1</sup> hereinafter referred to as the "Act", and the Regulations issued pursuant thereto (12 F. R. 4331). Jurisdiction of the Court below was invoked pursuant to Section 206 (b) of said Act.

On November 16, 1948 the Housing Expediter filed suit against the defendant as landlord of premises located at 1925-1953 Jackson Street, San Francisco, California (R. 1). The housing accommodations in

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<sup>1</sup> Sections 206 (a) and (b) of the Act are set forth in full (*infra*, p. 32).

question were located within the San Francisco Bay Defense-Rental Area and were subject to the Act and the regulations issued pursuant thereto. The defendant-landlord was sued for an injunction restraining him from violating said Act and regulations and for an order of restitution returning rents unlawfully collected (R. 3-4).<sup>2</sup> The defendant denied generally the collection of rents in excess of the legally established maximum (R. 7), and as an affirmative defense pleaded compliance with Section 204 (b) of the said Act,<sup>3</sup> stating that the rents collected were the permissible 15% increase in the monetary rents allowable under said Act (R. 8).

It was the plaintiff's contention at the outset of the trial that these leases were not "valid leases" within the meaning of Section 204 (b) because they provided for a decrease of services contrary to the requirements of the Act and the regulation. Plaintiff contended that these leases did in fact provide for a decrease in services inasmuch as they contained a shifting of the landlord's obligation to maintain the premises to the tenant (Tr. 2). The crux of the matter turned upon whether or not the handwritten guarantee initialed "JC," after Clause 19, was a part of the leases prior to their rejection by the Housing Expediter (Plaintiff's Exhibit No. 1). This guarantee reads: "Lessor agrees to maintain same services as before signing of this lease." The defendant main-

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<sup>2</sup> At the time of trial defendant no longer owned or operated the property so the prayer for injunction was abandoned (Conclusion 4, R. 15).

<sup>3</sup> Section 204 (b) is set forth in full (*infra*, p. 31).

tained that this statement was in the leases *prior* to the signing and filing of these leases (Tr. 97). However, on cross-examination plaintiff introduced into evidence a letter dated December 10, 1948 written by defendant's attorney and addressed to Mr. Sidney Feinberg, Chief of the Litigation Section of the Office of the Housing Expediter in San Francisco (Plaintiff's Exhibit No. 5) which refuted such contention. This letter reads as follows (Tr. 108-110):

Mr. DONOHUE. This letter is addressed to Mr. Sidney Feinberg, dated December 10, 1948:

Re: *Woods v. Cornet*, Action # 28433-R

DEAR MR. FEINBERG: For your records, we are herein setting forth the facts pertaining to the above entitled case.

On July 25, 1947, our client, Mr. Jacob Cornet, filed with the San Francisco Rent Office leases providing for a 15% rental increase on all of the units mentioned in your complaint. Some months later, the said leases were returned to Mr. Cornet with a notice of rejection on the ground that the leases provided for a reduction of services. Upon receipt of the rejected leases, Mr. Cornet went to each tenant and added the following clause in both the landlord's and tenant's copy of said leases, "Lessor agrees to maintain same services as before signing of this lease."

Mr. Cornet had originally obtained these form leases from the Apartment House Owners Association. After the above service clause was added to said leases, our client called the said association and talked to Mr. Christin who informed Mr. Cornet that it was not neces-



sary to refile the said leases. He told Mr. Cornet that as long as he originally filed the leases the O. P. A. had no right to return them and that Mr. Cornet had complied with the rent law by filing the same and there was nothing further that he had to do.

The original lease for 1941 Jackson was with a Mrs. Williams who moved out on or about the end of January, 1948, thereby decontrolling said unit. Mr. Cornet being advised that said unit was no longer under control rented the same to Mr. Farban at the increased rental.

Mr. Cornet sold this property in May of 1948.

On the basis of the above facts, we feel that this suit should be dismissed and no restitution required.

While you are giving this matter your consideration, please extend the time for the defendant to plead until January 15, 1948.

Very truly yours,

DAVID D. WEXLER.

The case was tried on the factual issues and decided in favor of the Expediter. In accordance with the testimony introduced, the Court below entering findings of fact as follows:

1. That the premises were subject to the Act and the regulations (R. 10).
2. That the maximum rent was as alleged in plaintiff's complaint (R. 11).
3. That the landlord collected specific amounts in excess of those established maxima which were set forth individually in said findings (R. 12).
4. That except as to one housing accommodation the excess rents collected by the defendant were collected

pursuant to a lease purported to have been executed pursuant to Section 204 (b) of the Act (R. 12).

5. Each of the leases mentioned above purported to have been executed on July 15, 1947 were received in the area rent office on July 25, 1947, and upon their examination in said office in the months of August and September 1947 were rejected by the area rent director "as not conforming with the requirements of the Act and were returned to the defendant as not acceptable" for filing, and in which the reasons for such rejection were set forth (R. 13).

6. That after said rejection and notice to the defendant he took no administrative appeal or review and failed, neglected or refused to file new, modified or corrected leases and continued to collect the rents provided in the rejected leases (R. 13).

7. That the reasons for rejection of the leases by the Area Rent Director are supported by substantial evidence (R. 14).

8. That the leases above mentioned, "were ineffective to increase the legal maximum rent for the accommodations" because "each of said leases contained provisions permitting or providing for a substantial decrease or reduction in services" (R. 14).

9. That defendant no longer owns or operates the housing accommodations in question (R. 14).

As conclusions of law the Court held:

1. That the Court had jurisdiction of the subject matter and of the parties (R. 14).

2. That defendant has both failed to pursue and exhaust prescribed administrative remedies (R. 15).

3. "That the leases \* \* \* were not valid or

effective to increase the legal maximum rent \* \* \*” (R. 15).

4. That plaintiff is not entitled to an injunction because defendant no longer owns or operates the premises (R. 15).

5. That on account of the violations of the Act and the regulations, an order of restitution be entered requiring the return of the excess rents to the tenants so overcharged (R. 15).

On the basis of the foregoing, the Court below entered a judgment on June 1, 1949 providing for the return of the excess rents collected to specifically named tenants in the total sum of \$821.14 (R. 17). Notice of appeal was filed on July 28, 1949.

#### STATUTES AND REGULATIONS

The issues in this appeal turn upon the provisions of the Act and the regulations regarding:

1. The permissive increase in rent provided in Section 204 (b) of said Act where tenant and landlord enter into a voluntary written lease for a given statutory period, and

2. Whether the maximum rent as used in the Act and regulation is confined to the monetary rent involved or whether it includes the term as used in its full connotations in both the Act and regulation; that is, whether a decrease in services is an increase in rent as to invalidate a monetary increase in rent of 15% authorized by the Act.

The pertinent portions of the Act are:

Section 204 (b) (50 U. S. C. A. 1894 (b), *infra*, p. 31), which provides that the maximum rent is the

maximum rent in effect on June 30, 1947 unless the landlord and tenant (1) voluntarily enter into a written lease on or before December 31, 1947, (2) the lease takes effect after July 1, 1947 and expires on or after December 31, 1948, (3) if such lease is filed within fifteen days of execution with the Housing Expediter, (4) the rent may increase not more "than fifteen per centum over the maximum rent \* \* \*." Such lease being validly filed with the area rent director removes said property from federal rent control.

Section 204 (d) (50 U. S. C. A. 1894 (d), *infra*, p. 32) provides that the Housing Expediter may issue such regulations as are consistent with Title II of the Act and necessary to carry out the provisions of Section 204.

Section 206 (a) (50 U. S. C. A. 1896 (a), *infra*, p. 32) provides that it shall be unlawful for any person to demand, accept, or receive any rent in excess of the maximum established under Section 204.

Section 206 (b) (50 U. S. C. A. 1896 (b), *infra*, p. 32) provides that the Expediter may apply for an injunction and "other order" in order to enforce compliance with said Section 206 (a).

Pertinent provisions of the Controlled Housing Rent Regulation (12 F. R. 4331) are set forth in full, *infra*, pp. 33-35, and are summarized as follows:

Section 1 of said regulation defines "Rent" as "the consideration, including any bonus, benefit, or gratuity, demanded or received for or in connection with the use or occupancy of housing accommodations or



the transfer of a lease of such accommodations.”

Section 2 of said regulation provides that no person shall demand, accept, or receive rent in excess of the legally established maximum and further provides that “a reduction in the minimum space, services, furniture, furnishings or equipment required under Section 3 of this regulation shall constitute an acceptance of rent higher than the maximum rent \* \* \*.”

Section 3 provides that every landlord must provide the same living space as provided on June 30, 1947, and the same essential services, furniture, furnishings, and equipment as he was required to provide on that date.

Section 4 (a) of the regulation provides that the maximum rent shall be that which was in effect on June 30, 1947, as established under the Emergency Price Control Act of 1942.

Section 4 (b) of the Controlled Housing Rent Regulation (12 F. R. 4331), consistent with the provisions of Section 204 (b) of said Act provides for the carrying out of the enumerated provisions of Section 204 (b) and the addition provides that “a lease shall be effective under this paragraph to increase the maximum rent only if it provides with the housing accommodations the same living space and the same essential services, furniture, furnishings, and equipment as required by this regulation prior to the effective date of the lease \* \* \*.”



## ARGUMENT

## I. Contrary to defendant's first contentions the rent regulation is consistent with the act

A. A cursory examination of the Act, the regulations and the cases construing them will amply demonstrate that Section 4 (b) of the regulations is consistent with the Act. The Housing and Rent Act of 1947 provided *inter alia* that the Expediter may "by regulation or order, make such adjustments in such maximum rents as may be necessary to correct inequities or further to carry out the purposes and provisions of this title \* \* \*" (Sec. 204 (b)). Pursuant to his statutory authority "to carry out the provisions of this title", the Expediter promulgated the "Controlled Housing Rent Regulation" (hereinafter referred to as the "Regulation") (12 F. R. 4331). Section 2 (a) of said Regulation provides that a reduction in essential services shall constitute an increase in rent. Section 2 (a) provides as follows:

*Prohibition against higher than maximum rents—(a) General prohibition.*—Regardless of any contract, agreement, lease, or other obligation heretofore or hereafter entered into, no person shall offer, demand or receive any rent for or in connection with the use or occupancy on and after the effective date of this regulation of any housing accommodations within the Defense-Rental Area higher than the maximum rents provided by this regulation; and no person shall offer, solicit, attempt, or agree to do

any of the foregoing. A reduction in the minimum space, services, furniture, furnishings, or equipment required under section 3 of this regulation shall constitute an acceptance of rent higher than the maximum rent. Lower rents than those provided by this regulation may be demanded or received.

The Regulation further provides that the landlord shall continue to furnish minimum services. Section 3 reads:

\* \* \* every landlord shall, as a minimum, provide with housing accommodations, the same living space as provided June 30, 1947, or on the date he first rented on or after July 1, 1947, and the same essential services, furniture, furnishings, and equipment as those he was required to provide on June 30, 1947, in accordance with the Rent Regulation for Housing, issued pursuant to the Emergency Price Control Act of 1942, as amended, or those he provided on the date he first rented on or after July 1, 1947, and as to other services, furniture, furnishings and equipment not substantially less than those he was required to provide on June 30, 1947, or actually provided on the date of first renting on or after July 1, 1947.

There can be no serious contention made that under the Housing and Rent Act of 1947 the Expediter lacks power to issue regulations and orders to achieve "a reasonable stability in the general level of rents \* \* \*" (Sec. 201 (b)). In so issuing these regulations, he is limited only by the intent of the Act, and the means to effectuate that intent so long as they are neither unreasonable nor capricious (*Commissioner of*

*Internal Revenue v. Fiske's Estate*, 128 F. 2d 487, 490 (C. A. 7th)). As was said in that case:

In construing a claimed exemption, we must consider the objects and purposes of the statute and give it such a construction as will carry out the true intent and meaning of Congress.

In applying these tests, we may look to the history of these provisions and the Court's interpretation and application of them.

Both Sections 2 and 3 above (pp. 9-10) were promulgated in substantially the same form (8 F. R. 7322) under the Emergency Price Control Act of 1942, as amended (50 U. S. C. A. 901, et seq.)<sup>4</sup> as Sections 2 and 3 of the Regulation under the Housing and Rent Act of 1947. Section 2 was less explicit under the prior Act than under the present Act in that the sentence "a reduction in the minimum space, services,

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<sup>4</sup> The pertinent provisions of the Regulation issued pursuant to the Emergency Price Control Act, as amended (50 U. S. C. A. 901, et seq.) provided that "no person shall demand or receive any rent for or in connection with the use or occupancy on or after the effective date of regulation of any housing accommodations within the Defense-Rental Area higher than the maximum rents provided by this regulation \* \* \*" (Sec. 2 (a)). Within the meaning of that section, "rent" was defined as "the consideration including any bonus, benefit or gratuity demanded or received for or in connection with the use or occupancy of housing accommodation \* \* \*" (Sec. 13 (a) (10)). That definition has been adopted by the Regulation issued pursuant to the present Act (Sec. 1, 12 F. R. 4331). As a means of assuring that each tenant would not indirectly suffer from actual cost increases while paying same monetary rent, the Administrator provided "except as set forth in Section 5 (b), every landlord shall as a minimum provide with housing accommodations \* \* \* the same essential services, furniture, furnishings and equipment as those provided on the date determining the maximum rent \* \* \*" (Sec. 3).

furniture, furnishings, or equipment required under Section 3 of this Regulation shall constitute an acceptance of rent higher than the maximum rent," was not part of it. Even though that express *caveat* was not part of the original Regulation, the courts had no hesitancy in determining that a decrease in services was an increase in rent.

This contention has been recognized by the Emergency Court of Appeals, the enforcement courts, and by the Price Administrator in the administration of the Price Control Act (*Benenson Realty Corp. v. Porter*, 158 F. 2d 163 (E. C. A.); *Absar Realty Company v. Bowles*, 149 F. 2d 654 (E. C. A.); *Porter v. Darlington*, 158 F. 2d 68 (C. A. 10th); *Woods v. Hadesman*, 86 N. E. 2d 583 (Ill. App.)). There can be little question from these cases that the discontinuance of service, furniture, and furnishings is an increase in rent within the meaning of the Act and the Regulations issued thereunder, and likewise for all practical purposes, that the Regulation is perfectly consistent with the Act. Nor can there be any doubt but that defendant contends that a reduction in services is not an increase in rent. He states this unequivocally on page 13 of his brief:

It is our contention that where the leases comply with all of the provisions of the Act, as in this case, that the new and increased maximum rent went into effect August 1, 1947; that the Area Rent Director had no authority to reject said leases on August 14, 1947, and September 8 or 9, 1947, and that the lower Court erred in holding that even though the leases complied with all of the provisions of the



Act that because said leases provided for reduction of services that by virtue thereof said leases were ineffective to increase the legal maximum rental.

Under the Emergency Price Control Act of 1942, the Emergency Court of Appeals frequently upheld the validity and propriety of administrative orders reducing rentals where services were reduced (see, *Benenson Realty Corp. v. Porter*, 158 F. 2d 163; *Absar Realty Company v. Bowles*, 149 F. 2d 654). The manifest reasoning behind this rule was that reduction of services constituted an increase in rent. This was consistently the rule adhered to by the Price Administrator under the Act: "If the tenant is required to pay the same rent and receives less services, it is as much an increase in rent as the payment of a higher rent for the same services would be" (*In the Matter of Herman Landerman*, Docket No. RPA-VI-73-P, 4 OPA Op. & Dec. 3233, 3236). Again, *In the Matter of Frederick Bartenstein*, Docket No. RPA-VIII-82-P, OPA Op. & Dec. 3392, the Administrator said:

The control of services under the regulation is exercised primarily for the purpose of assuring that the landlord does not in effect increase the maximum rent by a decrease in services. A withdrawal of services has much the same practical effect as an increase in rent.

Furthermore, the Emergency Court of Appeals held that a reduction in services justified a decrease in rent in the *Benenson* case, 158 F. 2d 163, where services were reduced, and an order decreasing the rent was entered:



The reason for making the decrease in rentals thus effective was because the services had been discontinued while the premises were occupied, without orders having been secured permitting the decrease of services, and without a showing that it was impossible for the landlord to maintain the services (p. 164).

So, too, in vindication of the public interest, enforcement courts have not hesitated to exercise both their traditional equity powers, and also the statutory powers granted by the Emergency Price Control Act. A notable illustration is *Porter v. Darlington*, 158 F. 2d 68 (C. A. 10th), where the Court compelled a landlord to restore cooking gas services.

In the case of *Creedon v. Stratton*, 74 F. Supp. 170 (D. C. Neb.), the first case arising under the present rent Act, Judge Delehant expressly held that decrease in services was an increase in rent. In that case, as in the case at issue, the Expediter filed suit pursuant to Section 206 (b) for a mandatory injunction to restore discontinued services. The Court held that the suit was properly filed under Section 206 (b), holding that a decrease in services is an increase in rent.

This suit was expressly bottomed on Section 206 (b) of the Housing and Rent Act of 1947. That section must be carefully read in an appraisal of the extent to which the Expediter may demand injunctive relief as his right. It is only in the face of the actual or threatened violation by a person of Section 206 (a) of the Act forbidding the offering, solicitation, demanding, acceptance or receipt of overceiling rent, that the expediter may apply to the court

for relief. And the relief for which he may apply is narrowly defined as “an order enjoining such act or practice, or \* \* \* an order enforcing compliance with” Section 206 (a). And the court, upon a showing of such actual or threatened overceiling charge (*including, of course, overcharges through the interception or curtailment of service*), is directed to grant without bond “a permanent or temporary injunction, restraining order, or other order” (*Creedon v. Stratton*, 74 F. Supp. at p. 181). [Italics added.]

See also, *Creedon v. O'Brien*, No. C. A. 6782 (U. S. D. C. Mass.), decided May 16, 1947, not reported, for opinion see Appendix, p. 37.

B. The background of Section 4 (b) of the regulation is equally persuasive in view of the reenactment of the Act at a time when the Expediter's interpretation was in existence which declared that to be eligible for the benefits of Section 4 (b) a landlord could not reduce services. This is to be found in the official interpretation of Section 4 (b) which was published in the Federal Register on July 23, 1947 (12 F. R. 5040). In that interpretation the Expediter provided as follows:

VI. *Lease providing for decrease in living space, services, furniture, furnishings and equipment.*—In order for a lease to effectively increase the maximum rents otherwise allowable, it must be based upon the continuation of the same services by the landlord. Therefore, if a lease provides for a decrease in the living space or essential services, furniture, furnishings, or equipment which are required

under the regulations to be provided with the housing accommodations, or a substantial decrease in the other services, furniture, furnishings, or equipment, such lease shall be ineffective to establish a new maximum rent.

With the regulation in existence and the official interpretation having been published,<sup>5</sup> the Congress not only reenacted the provision of the statute in substantially the same term but did so after a thorough examination of the effect of the original enactment and the Expediter's administration under it. In reporting the bill to the House of Representatives the Committee on Banking and Currency stated:

In the second category there are those cases where such a 1947 lease might be terminated after the effective date of this act and prior to March 31, 1949. In these cases the Committee amendment provides that such housing accommodations remain subject to a maximum rent not to exceed 15 percent over the maximum rent which in the absence of a lease would be in effect with respect thereto on the effective date of this act.

This Court has held that such reenactment after Congressional scrutiny amounts to a legislative ratifi-

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<sup>5</sup> "This interpretation is controlling and should not be ignored unless plainly erroneous" (*Woods v. Macken*, No. 5941 (C. A. 4), decided December 19, 1949, citing *Bowles v. Seminole Rock and Sand Company*, 325 U. S. 410, 414; *Bowles v. Mannie & Co.*, 155 F. 2d 129, 133 (C. A. 7); *Porter v. Crawford & Doherty*, 154 F. 2d 431 (C. A. 9), certiorari denied 329 U. S. 720. As this Court said in the latter case "since such administrative construction is not irrational its interpretations are binding upon the courts") (p. 433).

cation of the administrative action. In *Bowles v. Wheeler*, 152 F. 2d 34, certiorari denied 66 S. Ct. 265, this Court stated:

The reenactment of the Act after such administrative construction was made known to Congress constitutes a legislative ratification of that interpretation.

See also *Woods v. Oak Park Chateau Corp.*, No. 9821, decided January 4, 1950 (C. A. 7th); *Bowles v. Griffin*, 151 F. 2d 458 (C. A. 5); *Pinkus v. Porter*, 155 F. 2d 90, 93 (C. A. 7).

The Third Circuit Court of Appeals applied the same rule to the lack of Congressional change to an administrative regulation. This statement of the rule is four-square to the case at bar:

Added sanction is given to the administrative interpretation by the reenactment of the statute without disapproval of the regulations thereunder (*Bazley v. Commissioner of Internal Revenue*, 155 F. 2d 237, 242 (C. A. 3)).

In view of the foregoing appellant's contention that the reasonable requirements of the regulation are beyond the Office of the Housing Expediter is unfounded and specious.

**II. There is no merit in defendant's third contention that the Court erred "in its finding that each of said leases contains provisions for permitting or providing for substantial decrease or reduction in services"**

Defendant's third contention challenges the finding of the Court below that the leases which he attempted to file contained a provision for a decrease in services. The appellant argues that the Court below erred on



two grounds in finding the leases properly rejected because they provided for a reduction in services:

1. Because the leases contained a "positive statement thereon that the landlord agrees to maintain the same services as before" (Br. 21), and

2. Because the landlord did not in fact reduce the services (Br. 22).

These contentions are clearly without merit.

1. The nub of defendant's argument in this case is that an unlawful reduction in essential services as provided in the leases in question did not constitute an increase in rent so that when added to the 15% monetary increase therein provided, the total increase was not in excess of the increase lawfully provided by Section 204 (b) of the Act and Section 4 (b) of the regulation. There is no question, of course, but that the leases actually provided for a decrease in services and that the findings of the Court below (R. 14) were supported by substantial evidence. Such finding must be accepted by this Court. (Rule 52 (a), Federal Rules of Civil Procedure (28 U. S. C. A., following Section 723 (c); *Columbian Nat. Life Ins. Co. v. Quandt & Sons*, 154 F. 2d 1006 (C. A. 9); *Coffin-Reddington v. Porter*, 156 F. 2d 113 (C. A. 9th); *Martini v. Porter*, 157 F. 2d 35 (C. A. 9th), certiorari denied 67 S. Ct. 109).

The record clearly shows and the Court below found that the landlord did not include a statement in the leases as alleged by him in his brief that he would continue "to provide substantially the same services, furnishings and equipment as those included in the maximum rent in Item 4" (Br. 21).



Plaintiff's Exhibit No. 5 was a letter dated December 10, 1948 from appellant's attorney to Mr. Sidney Feinberg, Chief, Litigation Section of the Office of the Housing Expediter in San Francisco<sup>6</sup> (Tr. 110). In that letter to Mr. Feinberg which was "for your records" (Tr. 108) appellant's attorney stated:

On July 25, 1947, our client, Mr. Jacob Cornet, filed with the San Francisco Rent Office leases providing for a 15% rental increase on all of the units mentioned in your complaint. Some months later, the said leases were returned to Mr. Cornet with a notice of rejection on the ground that the leases provided for a reduction of services. Upon receipt of the rejected leases, Mr. Cornet went to each tenant and added the following clause in both the landlord's and tenant's copy of said leases, "Lessor agrees to maintain same services as before signing of this lease."

\* \* \* \* \*

This document was carefully weighed by the Court below in arriving at his conclusion that the original leases had in fact been rejected from filing because of the provision for a decrease in services. The Court clearly indicated that the information contained in the letter must have been furnished by the defendant.

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<sup>6</sup> There was some attempt at the trial to disparage the role of David Wexler as attorney for defendant (Tr. 108-112); and that there was a misunderstanding between them (Tr. 115). However, the Record shows that David Wexler not only wrote the letter on information furnished by defendant on December 10, 1948 (Tr. 110), but also prepared and filed the answer on said information on January 31, 1949. The answer was filed presumably after Mr. Louis Wexler had returned to his office and reviewed it (Tr. 106).

The COURT. Did you show him this letter?

Mr. WEXLER. Yes, I did, a copy of it, and he denied that is the conversation that he stated to my brother, that there was a misunderstanding of what he was trying to say.

The COURT. It follows he could not get that information from anyone else. Your brother could not get that, on the date of this letter.

The WITNESS. Maybe he misunderstood me. That could happen.

The COURT. I do not think he misunderstood you at all, for the record discloses clearly what is in this letter. They have been changed, and they were changed after the OPA rejected them. The reason I develop these facts, I do not want to interfere with the trial of any case, but if there is any doubt about it at all you can make any kind of a showing you see fit. Is that all from this witness? (Tr. 115-116).

The letter referred to was introduced on cross-examination of the defendant for the purpose of impeaching his testimony on this point. The Court below had the opportunity to observe the conduct of the defendant on the stand and to weigh his oral testimony against this documentary proof and decided to accept the document. The inferences drawn therefrom by the Court below, being supported by substantial evidence must be accepted by this Court.

The trial court observed their conduct and demeanor while on the stand, and was in better position than we are to appraise the situation and to draw inferences. We are not able to

say that the finding in question was clearly erroneous and are therefore obliged to accept it. *Columbian National Life Ins. Co. v. A. Quandt & Sons*, 9 Cir., 154 F. 2d 1006. (*Coffin-Reddington v. Porter*, 156 F. 2d 113, 114 (C. A. 9th).)

On the basis of the foregoing evidence and the authorities heretofore cited appellant clearly failed to establish that the Court below erred in finding that the leases did in fact provide for a reduction in service.

2. Defendant's contention that he did not in fact reduce the services is beside the point in determining whether he is entitled to the benefits of the Act. The Expediter filed suit for the collection of excess rents. The landlord contended that the rents were being collected pursuant to statutory authority. In the Court below the Expediter proved to the satisfaction of the Court that the leases supporting the rent increases were contrary to the express provisions of the Act and the regulation. Therefore, the point at issue was not whether the services had in fact been reduced. The question solely before the Court below was whether the leases were properly rejected as not conforming to the Act and the regulations.

This Court and other courts of appeal have held that where a statutory exemption or benefit is made available under certain conditions, the person claiming such benefit must strictly follow the requirements of the statute. In *Fontes v. Porter*, 156 F. 2d 956 (C. A. 9), the Price Administrator sued for over-

charges because the defendant had sold a rebuilt tool at the "rebuilt and guaranteed price" without providing a written guarantee required by the Regulation as a condition to charging such price. The seller pleaded *inter alia* that he orally guaranteed the tool and in pursuance of such guarantee had actually serviced it. In rejecting that defense this Court speaking through Judge Healy said at p. 958:

Neither of these requirements was met by appellant. In the absence of compliance he was not entitled to take advantage of the price permitted for rebuilt and guaranteed tools. A holding otherwise would encourage equivocation and evasion.

Such was the conclusion of the Court of Appeals for the First Circuit in *Porter v. Nowak*, 157 F. 2d 824. In that case the seller had disposed of a motor vehicle at a guaranteed price without furnishing a written guarantee. He did, however, furnish an oral warranty in pursuance of which he serviced the car on two separate occasions. In holding that the dealer had in fact overcharged because of failure to furnish a written guarantee, the Court of Appeals said that there was good and sufficient ground for adhering to the statutory provisions and that failure to follow them rendered the seller liable for such failure.

The rule expressed by this Court in the *Fontes* case, *supra*, has been applied by the courts in construing Section 204 (b) of the Act of 1947, as amended. Failure to comply with the strict filing requirements of the statute was a fatal defect (*Woods v. Roberts*, No. 9024 (E. D. Pa.), decided 2/21/49, opinion set forth in full, *infra*, pp. 41-42).



However, it is well settled that to effectuate a valid and legal increase in the maximum legal rent there must be compliance with the Administrative procedure as contained in the Act and a failure so to do is fatal in an action such as is presently before this Court (*infra*, p. 42).

The leases increased the rent and if in compliance with the Act decontrolled the property.<sup>7</sup> The literal provisions of both the Act and the regulations have been upheld by many other courts. The following cases have upheld this principle but have not published their opinions: *Woods v. Gossett*, No. 3259 (M. D. Pa.), decided 12/10/48; *Woods v. Davidson*, No. 862 (S. D. Tex.), decided 3/14/49; *Woods v. Hustad*, No. 375 (D. Mont.), decided 2/28/49; *Woods v. Wald Opticians* (E. D. Pa.), No. 4524, decided 10/18/48; *Woods v. Tiffany* (N. D. N. Y.).

As Judge Murphy said in the *Gossett* case, *supra*:

The regulations are in accord with the Act itself and clearly and specifically enunciate the intent of Congress. See U. S. Code Congressional Service, 80th Congress, First Session 1947 at p. 1237 et seq., (Statement of the Managers on the Part of the House, House Report No. 591, June 13, 1947) particularly at p. 1240 discussing Section 204 (b) and stating clearly that the fifteen percent increase would be effective only if certain conditions were complied with, one of which was the requirement of filing in accordance with the requirements

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<sup>7</sup> It must be borne in mind that the signing of a voluntary lease decontrolled the property permanently (Sec. 204 (b)). A rigid adherence to the letter of the Act was necessarily within Congressional intent. (See H. Rep. 591, 80th Cong. 1st Sess., p. 12.)



spelled out in the Act. (The opinion in this case is set forth in full in the Appendix, *infra*, pp. 49-51.)

In the *Wald Opticians* case, *supra*, Judge Duffy (now Circuit Judge), stated among other findings of fact:

10. In none of these instances recited in Paragraph 8 have these leases entered into between the landlord and tenant been filed with the Housing Expediter as provided by the Housing and Rent Act of 1947, but were filed January 19, 1948.

11. The leases entered into between the landlord and the tenants are ineffective to increase the legal maximum rentals of the premises involved herein.

And in his conclusions of law he stated *inter alia* based upon the foregoing findings:

3. The leases entered into between the landlord and the tenants on September 1, 1947, are ineffective to increase the legal maximum rentals of the premises involved herein.

(The findings and conclusions of the case are set forth in full, *infra*, pp. 43-48.)

The appellant's failure to abide by the provisions of the Act, the regulation and the interpretation sustain the Expediter's rejection of the filing of the leases in question. On the authority of the foregoing opinions the Court below correctly held that the monetary rents collected by the appellant were in excess of the legally established maxima. Restitution was therefore the proper remedy to be applied by a court of equity. *Porter v. Warner Holding*

*Company*, 328 U. S. 395; *Woods v. Richman*, 174 F. 2d 614 (C. A. 9); *Woods v. Gochnour*, 177 F. 2d 964 (C. A. 9).

So here, the landlord's failure to adhere to the statute and regulations resulted in a rejection of his leases. His leases remained defective and no attempt was made by him to correct the defect or to appeal from such rejection. His failure to do one or both rendered him liable for the consequences of his illegal conduct and the Court below correctly so found.

### III. The Court below correctly held that defendant failed to exhaust his administrative remedies

If this Court agrees with appellee's argument in Points I and II above, it is unnecessary to consider defendant's argument that the Court below was in error in holding that the defendant failed to exhaust his administrative remedies (R. 15). The finding is supported by the record in the following examination of the Area Rent Attorney:

Mr. DONOHUE. Q. Mr. Goldberg, was there any right of administrative review to the Form D-27-A giving notice of the rejection of this lease?

A. There was.

Q. To whom did he have the right of appeal? State if you know.

A. He had the right of appeal both to the Regional Housing Expediter and to the National Housing Expediter.

Q. Could you state by virtue of what regulation?

A. By virtue of the Rent Procedural regulation No. 1 issued September 4, 1947.

Q. Do the records of your office indicate that any such right was ever exercised in connection with these premises?

A. Our records indicate that they were not.

Defendant argues in his Point II that the Court below was in error in finding defendant had failed to exhaust his administrative remedies, for two reasons:

1. Exhaustion of administrative remedies was unnecessary because the regulation was invalid, and

2. That the Area Rent Director did not issue an order from which a appeal could be taken but merely issued a "Notice of Rejection." As shown above (pp. 9-17) in Point I, the regulation is inconsistent with the Act. There is, therefore, no reason to re-argue that contention.

Thus, the remaining contention for consideration is that defendant was relieved of the duty to exhaust his administrative remedies because no order was issued but "merely a Notice of Rejection." The short answer to this contention is contained in the transcript in the colloquy between the Court and counsel, where the Court aptly points out that the objection is one of form and not of substance and that it was sufficient compliance with the Act and the regulation that the defendant was given actual Notice of Rejection of the leases and reasons for such rejection.

The COURT. If I followed you, you indicated there was no order set?

Mr. WEXLER. There was no order set. It was a notice on a form D-27a, a notice of return of the rejected lease.

Mr. DONOHUE. Counsel has reference to form and not to substance. I think if the court will read that——

The COURT. The record discloses it complies with the law.

Mr. WEXLER. That, to my mind, is not a formal order.

The COURT. You mean the form of it?

Mr. WEXLER. Yes, it is not an order, in a form in which the rent director makes an order.

The COURT. As far as this court is concerned, that is a sufficient order for all purposes here, and if I am in error about that you may point it out.

Mr. WEXLER. My experience with orders is that orders have always stated on their face, "This is an order of the area rent director," and that the order takes effect on a certain date.

The COURT. Not necessarily. Notice is all that is necessary. However, you may proceed.

Sections 840.11 through 840.16 of Procedural Regulation No. 1 (12 F. R. 5916)<sup>8</sup> provide for the procedure in obtaining rent increases by filing leases. Section 840.13 provides that where the rent director determines that the leases failed to conform to the statutory requirements "he shall return the lease to the landlord together with an order notifying the landlord that the lease has been rejected." Within

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<sup>8</sup> The validity of this regulation has been challenged by appellant (Br. 4). This regulation is merely procedural. Since he has challenged the substantial regulation (Sec. 4 (b)), the argument in support of the validity of Section 4 (b), *supra*, pp. 15-17, is basically applicable to the Procedural Regulation, therefore, it will not be reargued here.



thirty days of the receipt of such order, the landlord may ask for a review of such order "or appeal pursuant to Sections 824.23 or .25 and following." Sections 840.23 and .25 govern the review of a rent director's order by the Regional Housing Expediter. Upon failure to obtain relief from the Regional Housing Expediter, the landlord is permitted to appeal to the Housing Expediter.

Defendant for the first time raises the question of the fact that some of the leases were rejected prior to the issuance of the foregoing Procedural Regulation (Br. 20.) However, this belated defense to the failure to exhaust his administrative remedies is specious on the facts themselves and upon the proved conduct of the defendant. The provisions of the regulation (Section 840.14) permit a landlord to move within thirty days after rejection of his lease for a "reconsideration of such order" or "file an application for review." Since this regulation was issued on September 4, the leases which were rejected on August 8 and 9 could have been appealed or reconsidered pursuant to that section. Obviously the regulation was in effect for three of the leases since by defendant's own admission they were rejected on "September 8 or 9" (Br. 10).

In any event, defendant's true intent may be gathered from plaintiff's Exhibit No. 5, the letter written by Mr. David Wexler to Mr. Sidney Feinberg, *supra*, p. 3, in which Mr. Wexler states:

Mr. Cornet had originally obtained these form leases from the Apartment House Owners Association. After the above service clause



was added to said leases, our client called the said association and talked to Mr. Christin who informed Mr. Cornet that it was not necessary to refile the said leases. He told Mr. Cornet that as long as he originally filed the leases the O. P. A. had no right to return them and that Mr. Cornet had complied with the rent law by filing the same and there was nothing further that he had to do.

It would unnecessarily labor the point to enumerate the administrative procedure available to Mr. Cornet in view of his avowed intent and subsequent conduct as revealed by the foregoing statement.

The failure of the defendant to resort to administrative remedies provided by the Housing Expediter precluded defendant from claiming that the Area Rent Office was in error in rejecting his leases. As the Supreme Court held in *Yakus v. United States*, 321 U. S. 414, 435, a defendant must first exhaust his administrative remedies even in a criminal case where the defendant asserts the unconstitutionality of a regulation establishing maximum prices which he is charged with having violated. As stated by this Court in *La Verne Co-op. Citrus Ass'n. v. United States*, 143 F. 2d 415, at p. 419 (C. A. 9):

A study of relevant decisions leaves no doubt that an equity court has no jurisdiction to examine the validity of an administrative order where the administrative remedy has not been invoked or has not been completed and where the one harmed by the administrative order is the moving party in the equity action. *Locketty v. Phillips*, 319 U. S. 182, 63 S. Ct. 1019, 87 L. Ed. 1339; *Myers v. Bethlehem Shipbuilding*

*Corp.*, 303 U. S. 41, 58 S. Ct. 459, 82 L. Ed. 638; *United States v. Superior Court*, 19 Cal. 2d 189, 120 P. 2d 26.

See also, *Woods v. Durr*, 176 F. 2d 273 (C. A. 3d) where the challenge to a regulation was also made by way of defense.

Therefore, the defendant having failed to avail himself of his administrative remedies precludes his right to challenge the validity of the Notice of Rejection of his leases. "Courts before have refused to hear defendants on points susceptible of correction by administrative procedures." (*LaVerne Co-op. Citrus Ass'n. v. United States*, 143 F. 2d, at p. 420.)

#### CONCLUSION

It is respectfully submitted on the basis of the foregoing that the judgment of the Court below is correct and should be affirmed.

ED DUPREE,

*General Counsel,*

A. M. EDWARDS, JR.,

*Acting Assistant General Counsel,*

FRANCIS X. RILEY,

*Special Litigation Attorney,*

*Office of the Housing Expediter,*

*Washington 25, D. C.*

## APPENDIX

### HOUSING AND RENT ACT OF 1947 (50 U. S. C. APP. 1881 ET SEQ.)

SEC. 204. (b) During the period beginning on the effective date of this title and ending on the date this title ceases to be in effect, no person shall demand, accept, or receive any rent for the use or occupancy of any controlled housing accommodations greater than the maximum rent established under the authority of the Emergency Price Control Act of 1942, as amended, and in effect with respect thereto on June 30, 1947: *Provided, however,* That the Housing Expediter shall, by regulation or order, make such adjustments in such maximum rents as may be necessary to correct inequities or further to carry out the purposes and provisions of this title: *And provided further,* That in any case in which a landlord and tenant, on or before December 31, 1947, voluntarily enter into a valid written lease in good faith with respect to any housing accommodations for which a maximum rent is in effect under this section and such lease takes effect after the effective date of this title and expires on or after December 31, 1948, and if a true and duly executed copy of such lease is filed, within fifteen days after the date of execution of such lease, with the Housing Expediter, the maximum rent for such housing accommodations shall be, as of the date such lease takes effect, that which is mutually agreed between the landlord and tenant in such lease if it does not represent an increase of more than 15 per centum over the maximum rent which would otherwise apply under this section. In any

case in which a maximum rent for any housing accommodations is established pursuant to the provisions of the last proviso above, such maximum rent shall not thereafter be subject to modification by any regulation or order issued under the provisions of this title. No housing accommodations for which a maximum rent is established pursuant to the provisions of the last proviso above shall be subject after December 31, 1947, to any maximum rent established or maintained under the provisions of this title.

SEC. 204. (d) The Housing Expediter is authorized to issue such regulations and orders, consistent with the provisions of this title, as he may deem necessary to carry out the provisions of this section and section 202 (c).

SEC. 206. (a) It shall be unlawful for any person to offer, solicit, demand, accept, or receive any rent for the use or occupancy of any controlled housing accommodations in excess of the maximum rent prescribed under section 204.

SEC. 206 (b) Whenever in the judgment of the Housing Expediter any person has engaged or is about to engage in any act or practice which constitutes or will constitute a violation of subsection (a) of this section, he may make application to any Federal, State, or Territorial court of competent jurisdiction, for an order enjoining such act or practice, or for an order enforcing compliance with such provision, and upon a showing by the Housing Expediter that such person has engaged or is about to engage in any such act or practice a permanent or temporary injunction, restraining order, or other order shall be granted without bond.



## CONTROLLED RENT REGULATION FOR HOUSING (12 F. R. 4331)

SECTION 1. *Definitions and scope of this regulation.*— \* \* \* “Rent” means the consideration, including any bonus, benefit, or gratuity, demanded or received for or in connection with the use or occupancy of housing accommodations or the transfer of a lease of such accommodations.

SEC. 2. *Prohibition against higher than maximum rents*—(a) *General prohibition.*—Regardless of any contract, agreement, lease, or other obligation heretofore or hereafter entered into, no person shall offer, demand or receive any rent for or in connection with the use or occupancy on and after the effective date of this regulation of any housing accommodations within the Defense-Rental Area higher than the maximum rents provided by this regulation; and no person shall offer, solicit, attempt, or agree to do any of the foregoing. A reduction in the minimum space, services, furniture, furnishings, or equipment required under section 3 of this regulation shall constitute an acceptance of rent higher than the maximum rent. Lower rents than those provided by this regulation may be demanded or received.

SEC. 3. *Minimum space, services, furniture, furnishings and equipment.*—Except as set forth in section 5 (b), every landlord shall, as a minimum, provided with housing accommodations the same living space as provided June 30, 1947, or on the date he first rented on or after July 1, 1947, and the same essential services, furniture, furnishings, and equipment as those he was required to provide on June 30, 1947, in accordance with the Rent regulation for housing, issued pursuant to the Emergency Price Control Act of 1942, as amended, or those he provided on the date he first rented on or after July 1, 1947,



and as to other services, furniture, furnishings and equipment not substantially less than those he was required to provide on June 30, 1947, or actually provided on the date of first renting on or after July 1, 1947.

SEC. 4. *Maximum rents*—(a) *Maximum rents in effect on June 30, 1947.*—The maximum rent for any housing accommodation under this regulation (unless and until changed by the Expediter as provided in section 5) shall be the maximum rent which was in effect on June 30, 1947, as established under the Emergency Price Control Act of 1942, as amended, and the applicable rent regulation issued thereunder, except as otherwise provided in this section.

SEC. 4. (b) *Maximum rent established under a lease.*—In any case in which a tenant and landlord, on or before December 31, 1947, voluntarily enter into a valid written lease in good faith with respect to any controlled housing accommodations and such lease takes effect after July 1, 1947, and expires on or after December 31, 1948, the maximum rent for such housing accommodations shall be, as of the date such lease takes effect, the rent provided by the lease if it does not represent an increase of more than 15 percent over the maximum rent otherwise applicable. Such lease shall increase the maximum rent otherwise applicable for any housing accommodations only if a true copy thereof signed by both the landlord and tenant is filed with the area rent office for the Defense-Rental Area in which the accommodations are located within fifteen days after the date the lease is executed. Every landlord shall file with a true copy of such lease Form D-92—Registration of Lease—in triplicate. A maximum rent established under this paragraph shall not be subject to additional increase by execution of a subsequent lease. No maximum rent established

under this paragraph shall be subject to modification by any order of the Expediter.

A lease shall be effective under this paragraph to increase the maximum rent only if it provides with the housing accommodations the same living space and the same essential services, furniture, furnishings, and equipment as required by this regulation prior to the effective date of the lease, and as to other services, furniture, furnishings and equipment, not substantially less than required prior to the effective date of the lease. The landlord shall continue to provide such space and services, furniture, furnishings, and equipment at all times after the effective date of such lease.

## RENT REGULATION FOR HOUSING (8 F. R. 7322)

### SECTION 2 (a)

SEC. 2. *Prohibition against higher than maximum rents*—(a) *General prohibition*.—Regardless of any contract, agreement, lease, or other obligation heretofore or hereafter entered into, no person shall demand or receive any rent for or in connection with the use or occupancy on and after the effective date of regulation of any housing accommodations within the Defense-Rental Area higher than the maximum rents provided by this regulation; and no person shall offer, solicit, attempt, or agree to do any of the foregoing. Lower rents than those provided by this regulation may be demanded or received.

SEC. 3. *Minimum services, furniture, furnishings and equipment*.—Except as set forth in section 5 (b), every landlord shall, as a minimum, provide with housing accommodations the same essential services, furniture, furnishings, and equipment as those provided on the date determining the maximum rent, and as to other services, furniture, furnishings and

equipment not substantially less than those provided on such date: *Provided, however*, That where fuel oil is used to supply heat or hot water for housing accommodations, and the landlord provided heat or hot water on the date determining the maximum rent, the heat and hot water which the landlord is required to supply shall not be in excess of the amount which he can supply under any statute, regulation or order of the United States or any agency thereof which ratifies or limits the use of fuel oil.

SEC. 5 (a). *Decrease in minimum services, furniture, furnishings and equipment*—(1) *Decrease prior to effective date*.—If, services provided for housing accommodations are less than the minimum services required by section 3, the landlord shall either restore and maintain such minimum services or, within 30 days (or, for housing accommodations within the Los Angeles Defense-Rental Area, within 60 days) after such effective date, file a petition requesting approval of the decreased services. If, on such effective date (or on December 1, 1942, where the effective date of regulation is prior to that date), the furnishings or equipment provided with housing accommodations are less than the minimum required by section 3, the landlord shall, within 30 days after such date, file a written report showing the decrease in furniture, furnishings or equipment.

SEC. 13. *Definitions*.—(a) When used in this regulation the term: \* \* \*

(10) "Rent" means the consideration, including any bonus, benefit, or gratuity, demanded or received for the use or occupancy of housing accommodations or for the transfer of a lease of such accommodations.

District Court of the United States  
District of Massachusetts

FRANK R. CREEDON, HOUSING EXPEDITER, OFFICE OF  
THE HOUSING EXPEDITER

*v.*

ANNA O'BRIEN

C. A. No. 6782. May 16, 1947

WYZANSKI, J. This is an application for a temporary injunction made by Frank R. Creedon, Expediter, Office of the Housing Expediter. The application is made pursuant to the provisions of Section 205 (a) of the Emergency Price Control Act of 1942, as amended, 50 U. S. C., App. Sec. 925 (a). The provisions of the relevant regulation, that is to say, the rent regulation for transient hotels, residential hotels, rooming houses and motor courts, known as Regulation No. 1388, most recently amended November 1, 1946, include the following regulation in Section 6 (a):

So long as the tenant continues to pay the rent to which the landlord is entitled, no tenant of a room within a hotel, rooming house or motor court shall be removed from such room, by action to evict or to recover possession, by exclusion from possession, or otherwise, nor shall any person attempt such removal or exclusion from possession, notwithstanding that such tenant has no lease or that his lease or other rental agreement has expired or otherwise terminated unless \* \* \*. [The exceptions, not being pertinent to this case, are not quoted.]

The defendant, Anna O'Brien, is a resident of Boston, Massachusetts. At all material times she has



been landlord of a rooming house at 95 Pinckney Street, Boston, Massachusetts, which is located in the Eastern Massachusetts Defense-Rental Area as that area is defined in the rent regulation to which reference has already been made and which is set forth in extenso in 8 F. R. 7334 and amendments subsequently published.

For over nine years Dr. Dickinson S. Miller has been an occupant of rooms at 95 Pinckney Street, Boston. He has continuously since and prior to March 1, 1942, occupied the first floor front room of the rooming house. He has also at various times occupied additional rooms.

In the summer of 1946, Miss O'Brien several times orally stated to Dr. Miller that he should move. In the fall of 1946 she gave him a written notice to move. Neither the oral notices nor the written notice were supported by any of the grounds recognized in Section 6 of the rent regulation as being valid grounds for the termination of a tenancy, with two possible exceptions. Miss O'Brien appears to have made complaint that Dr. Miller did not keep his rooms in the most orderly and tidy fashion that she could imagine and she also made complaint with respect to a particular mat in the public bathroom. Miss O'Brien has not appeared here to support either of those allegations, and from listening to Dr. Miller I am persuaded that his conduct upon the premises has not been such as to justify terminating his tenancy on the ground that he has violated the obligations of a tenant or that he has committed a nuisance. Being a man 78 years of age and being by profession a teacher of philosophy, a professor and lecturer in that field, it is not to be anticipated that he will keep his quarters looking as neat as a bandbox. The phrase "a quatre epingles" is not a common descrip-



tion of either septuagenarians or philosophers; and when Miss O'Brien rented the premises to Dr. Miller she undoubtedly knew that he was past middle age and engaged in professional pursuits which would distract him from housekeeping duties.

Miss O'Brien, having failed to induce Dr. Miller to leave by her oral requests and her written notice, has resorted to various aggravations. She has removed from his room a bed as well as certain other furniture which was there on March 1, 1942. To his embarrassment she has removed the window shade. She has cut off the electric power necessary for the proper lighting of the room which was there on March 1, 1942. She has, with the purpose of causing embarrassment to Dr. Miller and affording him less protection than he is entitled to, taken away from him the key to the room.

The record makes it abundantly clear that by contemptible indirection, Miss O'Brien has been attempting to remove or exclude from possession a tenant entitled to the protections afforded by the Emergency Price Control Act of 1942 and by the rent regulation for rooming houses.

Upon the basis of this finding, I conclude as a matter of law that the plaintiff, Frank R. Creedon, Expediter, Office of the Housing Expediter, is entitled to the temporary injunction for which he prays. That injunction shall be so drafted as to require the defendant, Miss Anna O'Brien and her successors as landlords and all those persons in active concert or participation with her who receive actual notice of this order by personal service or otherwise, to refrain from evicting or excluding Dr. Dickinson S. Miller from possession of the first floor front room of the rooming house at 95 Pinckney Street, Boston Massachusetts, so long as he complies with the obligations

specified in Section 6 of the rent regulation for rooming houses. The injunction shall also specifically direct Miss O'Brien to restore to the room all articles of furniture which were present in that room on March 1, 1942 (including the bed, the chairs, the lamps, the window shade, and like articles). The order shall direct the defendant O'Brien to restore to that room the degree of electric current and power and the number of electric light bulbs which were provided on March 1, 1942; and the order shall also provide that the defendant O'Brien shall restore to Dr. Dickinson S. Miller the key to the said room. The injunction shall also provide that the defendant O'Brien shall provide such bedclothes and such services in connection with cleaning the room and making the bed as were supplied on March 1, 1942.

NOTE.—I wish to add a note with respect to one point which has been raised by Dr. Miller. He states that recently the defendant O'Brien has placed outside his window mosquito netting which is not placed outside the window of any other tenant. It is his view that the defendant O'Brien placed that netting outside his window, to use his words, "In connection with the recent siege of the premises." He states also that during the period of conflict between him and the landlady, he used his window as a means for securing candles and food and the like through the window. Since it is my anticipation that the defendant O'Brien will obey the injunction in this case and that the hostilities which resulted in what was alleged to be a "siege" may be brought to an armistice if not to a peace, I do not feel that my injunction need go so far as to embrace the netting; but nothing that I have said is to be regarded as suggesting that the defendant O'Brien should continue to leave the netting at the window or that Dr. Miller should take

in his own hand the question of disposition of the netting. I have no doubt that the defendant O'Brien, after receiving the specific injunction which this Court proposes to issue, will not desire to come as near as maybe to violating it in order to find out whether she is in contempt.

In the United States District Court for the  
Eastern District of Pennsylvania

Civil Action No. 9024

(Filed February 21, 1949)

TIGHE E. WOODS, HOUSING EXPEDITER OFFICE OF THE  
HOUSING EXPEDITER, PLAINTIFF

*v.*

ISABEL E. ROBERTS, 35 EAST STEWART AVENUE,  
LANSDOWNE, PENNSYLVANIA, DEFENDANT

SUR MOTION FOR SUMMARY JUDGMENT

FEBRUARY 21, 1949.

WELSH, J. This is an action in which the Housing Expediter seeks a refund of overcharges to two tenants and an injunction restraining defendant from violating the Housing and Rent Act of 1947, 50 U. S. C. A. Appendix, Section 1881 et seq. After answer by the defendant the plaintiff filed a motion for summary judgment on the ground that the pleadings and admissions on file in the action show there is no genuine issue as to any material fact and no defense set forth in the answer is sufficient in law.

The record discloses that the maximum legal rent for the housing accommodations within the Philadelphia Defense-Rental Area designated as third-floor apartment, 35 East Stewart Avenue, Lansdowne, Pennsylvania, was \$35.00 per month. The defendant-landlord received rent for the use and occupancy of

the aforesaid housing accommodations from the tenants, Mr. and Mrs. Eugene A. Martin, in the amount of \$50.00 per month from August 1, 1947, to November 30, 1947, inclusive, and from the tenant, Gerald B. Ogle, Jr., in the amount of \$50.00 per month from December 1, 1947, to May 31, 1948, inclusive. It is clear, therefore, that the defendant received rents in excess of the maximum legal rent established by the Act and Regulation issued pursuant thereto.

The contention is that the defendant should be excused because she acted in good faith in that she entered into an agreement with each of the tenants increasing the rent by 15%, and in addition, she partially furnished the housing accommodations in question at the times in question.

There can be no dispute that an increase in the maximum legal rent is authorized by the Act if agreed to by the parties or the accommodations are furnished in whole or in part. However, it is well settled that to effectuate a valid and legal increase in the maximum legal rent there must be compliance with the Administrative procedure as contained in the Act and a failure so to do is fatal in an action such as is presently before this Court.

We conclude, therefore, that there is no genuine issue as to any material fact and no defense set forth in answer is sufficient in law, and the motion for summary judgment is accordingly granted.

An order may be presented providing for payment in the amount of \$60.00 to the tenants, Mr. and Mrs. Eugene A. Martin, and for the payment of \$90.00 to the tenant, Gerald B. Ogle, Jr., and for an injunction restraining defendant from violating the Housing and Rent Act of 1947.



In the District Court of the United States for the  
Eastern District of Wisconsin

Civil Action No. 4524

TIGHE E. WOODS, HOUSING EXPEDITER, OFFICE OF THE  
HOUSING EXPEDITER, FOR AND ON BEHALF OF THE  
UNITED STATES, PLAINTIFF

*vs.*

WALD OPTICIANS, INCORPORATED, A WISCONSIN CORPO-  
RATION, AND ALEX WALD, INDIVIDUALLY, DEFENDANTS

FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER  
FOR JUDGMENT

The above entitled matter came on for trial before the Honorable F. Ryan Duffy, one of the Judges of this Court, in the Federal Courts Building, Milwaukee, Wisconsin, on the 14th day of October 1948, at 9:30 a. m. Eugene T. Devitt appeared as attorney for the plaintiff, and the defendants were represented by David Beanor. In open Court, the attorneys for the plaintiff and the defendant stipulated that the defendants increase the rentals 15% over the legal maximum rent, on 8 units at 2224 West Fond du Lac Avenue, Milwaukee, Wisconsin, on July 1, 1947, without the execution of written leases. It was further stipulated that on September 1, 1947, the defendants executed written leases with the 8 tenants involved herein, increasing the rents 15% over the legal maximum rentals. It was further stipulated that duly executed copies of these leases were not filed with Office of the Housing Expediter within 15 days after their execution as provided by the Housing Rent Act of 1947, as amended. Further it was stipulated and agreed that duly executed copies of these leases were filed with the Office of the Housing Expediter on January 19, 1948. Upon the stipulation thus entered into



in open Court and upon plaintiff's Complaint, Amended Complaint and Request for Admissions, and upon defendant's Answer to Request for Admissions Answer, and upon all the files and records herein, and the Court having heard the arguments of counsel for plaintiff and for defendants and being fully advised in the premises, makes the following Findings of Fact, Conclusions of Law and Order for Judgment.

#### FINDINGS OF FACT

1. Tighe E. Woods is the duly appointed and qualified Housing Expediter, Office of the Housing Expediter.

2. The Court has jurisdiction, by reasons of Section 206 (b) of the Housing and Rent Act of 1947, as amended, hereinafter referred to as the "Act".

3. At all times mentioned herein, and on and after July 1, 1947, there was continuously in full force and effect issued pursuant to Section 204 of the Act, the Controlled Housing Rent Regulation (12 F. R. 4331), hereinafter called the "Controlled Regulation," establishing maximum rents for the use and occupancy of controlled housing accommodations within the Defense-Rental Area of Milwaukee, Wisconsin, which includes the premises herein located at 2224 West Fond du Lac Avenue, Milwaukee, Wisconsin. Section 4 of the Controlled Regulation establishes the maximum rent for any housing accommodations thereunder to be the maximum rent which was in effect on June 30, 1947, as established under the Emergency Price Control Act of 1942, as amended, and of the applicable rent regulations issued thereunder.

4. On June 30, 1947, and during the prior time or periods mentioned herein, there was continuously in full force and effect, pursuant to Section 2 (b) of the Emergency Price Control Act of 1942, as amended,

the Rent Regulation for Housing (8 F. R. 7322), hereinafter called the "Rent Regulation", establishing maximum rents for the use and occupancy of housing accommodations within the Defense-Rental Area of Milwaukee, Wisconsin, in which the premises herein involved were located and which were owned by the defendants.

5. The maximum rentals, prescribed by the Rent Regulation set forth in the preceding paragraph hereof, for eight of the dwelling units in the premises involved herein, were as follows:

Unit:	<i>Maximum rent</i>
1-----	\$42. 50 per month
3-----	42. 50 per month
4-----	42. 50 per month
5-----	42. 50 per month
10-----	42. 50 per month
12-----	42. 50 per month
13-----	42. 50 per month
14-----	45. 00 per month

6. The aforesaid establishment contains numerous rooms, apartments, or housing accommodation units included in which are dwelling units or housing accommodation units which constitute controlled housing accommodation units within the meaning of the Act and the Regulation. At all times material herein, said controlled rooms, apartments, or housing accommodation units have been and are now let and rented out to various tenants for dwelling units and the defendants have been collecting and receiving rents from the tenants for the use and occupancy of all the said controlled rooms, apartments, or housing accommodation units in said establishment.

7. The defendants have engaged, and are about to engage, in acts and practices which constituted or will

constitute violations of Section 206 (a) of the Act and of other provisions of law applicable in the premises.

8. The defendants, in violation of the said Regulation, and Section 206 (a) of said Act, and Section 4 of the said Price Control Act, did, beginning with on or about July 1, 1947, demand, receive and have been collecting as rent herein, from the tenants of the premises, for the use or occupancy thereof, amounts in excess of the maximum legal rents established therefor, by said Acts and Regulations. In all instances the defendants and all of the tenants included herein entered into leases on or about September 1, 1947, which leases increased the rental rates 15% over the established maximum rents. In all instances, defendants increased rentals for all of the tenants two months prior to the execution of the leases.

9. Section 204 (b) of the Housing and Rent Act of 1947 provides as follows:

\* \* \* *Provided, further,* That in any case in which a landlord and tenant, on or before December 31, 1947, voluntarily entered into a valid written lease in good faith with respect to any housing accommodations for which a maximum rent is in effect under this section and such lease takes effect after the effective date of this title and expires on or after December 31, 1948, and if a true and duly executed copy of such lease is filed within 15 days after the date of execution of such lease, with the Housing Expediter, the maximum rent for such housing accommodations shall be, as of the date such lease takes effect, that which is mutually agreed between the landlord and tenant in such lease if it does not represent an increase of more than 15 per centum over the maximum rent which would otherwise apply under this section \* \* \*.

10. In none of the instances recited in Paragraph 8 have these leases entered into between the landlord and tenant been filed with the Housing Expediter as provided by the Housing and Rent Act of 1947, but were filed January 19, 1948.

11. The leases entered into between the landlord and the tenant are ineffective to increase the legal maximum rentals of the premises involved herein.

12. The Court finds that the sums listed below were collected from the tenants listed and constitute rentals in excess of the legal maximum rentals. The overcharges were collected from July 1, 1947, through January 19, 1948. The Court further finds that the other four tenants involved herein have signed releases with the defendants and are not entitled to a refund. The Court further finds that the four tenants involved herein are not entitled to refunds from the defendants on and after January 20, 1948, the date on which said leases were filed with the Office of the Housing Expediter.

Unit	Tenant	Overcharges
1	Arnold Kohne.....	\$44.66
10	Celia Dobratz.....	44.66
12	William Engelfried.....	44.66
14	W. J. Parkins.....	47.25

13. That the enforcement of the Housing and Rent Act of 1947, as amended, and the justice and equity of the situation requires the defendants to make restitution of all amounts listed above collected and accepted by them from the tenants in excess of the maximum legal rentals therefor.

#### CONCLUSIONS OF LAW

1. That this Court has jurisdiction of the subject matter of this action and the parties hereto.



2. That the defendants since on or about July 1, 1947, have been violating the provisions of the Emergency Price Control Act of 1942, as amended, and the Housing and Rent Act of 1947, as amended, by demanding, accepting or receiving rent for the housing accommodations in excess of the rental permitted by the Acts and Regulations.

3. The leases entered into between the landlord and the tenants on September 1, 1947, are ineffective to increase the legal maximum rentals of the premises involved herein.

4. That unless restrained by this Court, the defendants will continue to demand, accept and receive rent for said housing accommodations in excess of the maximum legal rentals established therefor.

#### ORDER FOR JUDGMENT

It is hereby ordered that judgment be entered:

1. Enjoining and restraining the defendants and those acting for the defendants from soliciting, demanding, accepting or receiving any rent in excess of the maximum rent prescribed by the Controlled Housing Rent Regulation, as amended, or in excess of the maximum rent permitted by any other regulation or order adopted pursuant to the Housing and Rent Act of 1947, as amended.

2. Ordering and commanding the defendants to make restitution to the tenants of the amounts listed in the Findings of Fact.

Dated at Milwaukee, Wisconsin, this 18th day of October 1948.

Enter:

DUFFY,  
*United States District Judge.*



United States District Court for the Middle District  
of Pennsylvania

TIGHE E. WOODS, HOUSING EXPEDITER, OFFICE OF THE  
HOUSING EXPEDITER, PLAINTIFF

v.

JOSEPH GOSSETT, 620 SOUTH 23RD STREET, HARRISBURG,  
PENNSYLVANIA

No. 3259, Civil Action

MEMORANDUM

The Housing and Rent Act of 1947, 50 U. S. C. A. App. Sections 1881-1902, effective June 30, 1947, provided in Section 204 (b), 50 U. S. C. A. App. Section 1894 (b), inter alia, “\* \* \* That in any case in which a landlord and tenant, on or before December 31, 1947, voluntarily enter into a valid written lease in good faith with respect to any housing accommodations for which a maximum rent is in effect under this section and such lease takes effect after the effective date of this title and expires on or after December 31, 1948, and if a true and duly executed copy of such lease is filed, within fifteen days after the date of execution of such lease, with the Housing Expediter, the maximum rent for such housing accommodations shall be, as of the date such lease takes effect, that which is mutually agreed between the landlord and tenant in such lease if it does represent an increase of more than 15 per centum over the maximum rent which would otherwise apply under this section \* \* \*

On June 30, 1947, pursuant to the authority granted to the Housing Expediter in Section 204 (d) of the Act, Controlled Housing Rent Regulation was issued (12 F. R. 4331) effective July 1, 1947. Section 4 (b) of said regulation provided inter alia that “such lease shall increase the maximum rent otherwise applicable for any

housing accommodations only if a true copy thereof signed by both the landlord and tenant is filed with the area rent office for the Defense-Rental Area in which the accommodations are located within fifteen days after the date the lease is executed. Every landlord shall file with a true copy of such lease Form D-92—Registration of lease—in triplicate \* \* \*

On July 23, 1947, the general counsel of the Housing Expediter issued an interpretative bulletin (12 F. R. 5040) as to the aforesaid Section 4 (b) of the regulations. This bulletin provided inter alia, "In order that a lease may be effective under Section 204 (b) of the Act and Section 4 (b) of the rent regulations to increase the maximum rent otherwise allowable by an amount not to exceed fifteen percent, all of the following requirements must be met: \* \* \* (7) The landlord must file with the area rent office a true and duly executed copy of the lease, or a true and duly executed copy of a lease extension agreement to which is attached a copy of the lease being extended (certified to be a true copy) within fifteen days after the date of execution of the lease or extension agreement." And further in Part IV of said bulletin under the heading "Filing Requirements"—"Under the Act and the regulations, a lease shall not be effective to increase the maximum rent unless a true and duly executed copy of the lease is filed within fifteen days after the date of its execution \* \* \*" And in Part V. "A" lease is ineffective to increase the maximum legal rent if it increases the maximum legal rent which was in effect immediately prior to the effective date of the lease by more than fifteen percent."

The regulations are in accord with the Act itself and clearly and specifically enunciate the intent of Congress. See U. S. Code Congressional Service, 80th Congress, First Session 1947 at p. 1237 et seq, (Statement of the Managers on the Part of the House, House Report No.

591, June 13, 1947) particularly at p. 1240 discussing Section 204 (b) and stating clearly that the fifteen percent increase would be effective only if certain conditions were complied with, one of which was the requirement of filing in accordance with the requirements spelled out in the Act.

The defendant landlord entered into lease agreements with three of his tenants increasing the maximum rent 25 percent, 15 percent, and 13 percent, respectively. At no time did the landlord make any attempt whatever to comply with the filing requirements. He seeks to defend such failure by pleading ignorance of the provisions of the Act, the Regulations and the Bulletin. In fact, no attempt had been made by the landlord to comply with the registration requirements in effect prior to the 1947 Act.

Defendant, relying upon *Porter, Price Administrator v. Warner Holding Co.*, 1946, 328 U. S. 395, 66 S. Ct. 1086, 90 L. Ed. 1332, asks this Court in the exercise of its discretion to deny the prayer of the Housing Expediter that defendant be ordered to make restitution of the rents thus illegally collected. To grant defendant's requests would be to ignore the clear and definite intent of the Act and the Regulations. See "Some Reflections on the Reading of Statutes", Vol. 47, Col. L. Rev., May 1947, p. 527 et seq, article by Mr. Justice Frankfurter, particularly at pp. 528, 533, 534, 536.

We do not pause to consider whether a statute differently conceived and framed would yield results more consonant with fairness and reason. We take the statute as we find it. Cardozo, J. in *Anderson v. Wilson*, 1933, 289 U. S. 20, 27, 53 S. Ct. 417, 77 L. Ed. 1004.

We must bear in mind the language of the Supreme Court in *The Hecht Co. v. Bowles*, 321 U. S. 321 at 330, 64 S. Ct. 587, 88 L. Ed. 754, "We do not mean to imply

that courts should administer Section 205 (a) grudgingly." And again at 331, "The Administrator does not carry the sole burden of the war against inflation. The courts also have been entrusted with a share of that responsibility. And their discretion under Section 205 (a) must be exercised in light of the large objectives of the Act. For the standards of the public interest, not the requirements of private litigation, measure the propriety and need for injunctive relief in these cases. That discretion should reflect an acute awareness of the Congressional admonition that 'of all the consequences of war, except human slaughter, inflation is the most destructive' \* \* \* and that delay or indifference may be fatal."

See also *Shadid v. Fleming*, 10 Cir., 160 F. 2d 752, 753; *Porter v. Block*, 4 Cir., 156 F. 2d 264, 268, holding that a provision similar to that here under consideration should be liberally construed in order to carry out the purpose of Congress to control prices and to prevent destructive inflation.

On the subject of the lack of knowledge of the landlord that he was violating the laws and the regulations, see *Gilbert v. Thierry*, D. C. Mass., 58 F. Supp. 235, 242, affirmed 1 Cir., 147 F. 2d 603, 604; *Creedon v. Evangelisti*, D. C. E. D. Pa. 77 F. Supp. 538 at 540; *West v. Winston*, D. C. E. D. Pa., 8 F. R. D. 311 See also *Brown v. Hecht Co.*, App. D. C. 137 F. 2d 689 at 691.

An order or restitution is not a judgment for damages or for penalties. It compels compliance and is restoration of the status quo which falls within the recognized power of a court of equity. *Bowles v. Skaggs*, 6 Cir., 151 F. 2d 817, 821.

\* \* \* an order of restitution may be granted with or without a prohibitory injunction. *Creedon v. Randolph*, 5 Cir., 165 F. 2d 918 at 920.



Similarly judgment may be granted where restitution is the only relief allowed. *Woods v. Wallace*, D. C. E. D. Pa. 8 F. R. D. 140.

While no opinions were written two district courts have also taken the position that failure to comply with the filing requirements of the Act and the Regulations make the lease ineffective and deny the 15 percent increase. In the case of *Woods v. Robenco, Inc.*, Civil Action No. 1944, decided June 25, 1948, W. D. Wis., Stone J. (unreported opinion) the leases were not filed at any time; in the case of *Woods v. Wald Opticians, Inc. et al.*, Civil Action No. 4524, decided October 18, 1948, E. D. Wis., Duffy J. (unreported opinion) the leases were filed after the fifteen days for filing had expired.

On the question of exercise of discretion, see message of President Truman in connection with the signing of the Housing and Rent Act of 1947 in U. S. Congressional Service, *supra*, at p. 1867.

The problem before the court in *Porter, Price Administrator v. Warner Holding Co.*, 328 U. S. 395, *supra*, was the question whether or not the district court had the power to order restitution. Upon remand in the *Warner* case, the lower court's order compelling restitution was approved by the Eighth Circuit, 166 F. 2d 119, the court using the language at 121, "We see nothing unconscionable in an order which requires the defendant to restore to those from whom they were received gains exacted in violation of law."

Since the landlord is no longer in possession of the premises, the request for injunction will be denied; the prayer for summary judgment will be granted.

JOHN W. MURPHY,  
*United States District Judge.*

DECEMBER 10, 1948.





No. 12347

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United States  
Court of Appeals  
For the Ninth Circuit.

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UNITED STATES OF AMERICA,  
Appellant,  
vs.  
ALL AMERICAN AIRWAYS, INC.,  
Appellee.

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Transcript of Record

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Appeal from the United States District Court  
for the Southern District of California  
Central Division

**FILED**

OCT 28 1949

PAUL P. O'BRIEN,  
CLERK



No. 12347

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United States  
Court of Appeals  
For the Ninth Circuit.

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UNITED STATES OF AMERICA,  
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Transcript of Record

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Appeal from the United States District Court  
for the Southern District of California  
Central Division





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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS:

For Appellant:

JAMES M. CARTER,

United States Attorney,

E. H. MITCHELL,

EDWARD R. McHALE,

Assistants U. S. Attorney,

EUGENE HARPOLE,

ROBERT D. SCOTT,

JAMES D. PETTUS,

Special Attorneys, Bureau of Internal  
Revenue,

600 U. S. Post Office & Court House  
Bldg.

Los Angeles 12, Calif.

For Appellee:

GUTHRIE, DARLING & SHATTUCK,

737 Pacific Mutual Bldg.

Los Angeles 14, Calif. [1\*]

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\* Page numbering appearing at bottom of page of original certified Transcript of Record.

In the District Court of the United States in and  
for the Southern District of California, Central  
Division

No. 8860-W

ALL AMERICAN AIRWAYS, INC., a Corpora-  
tion,

Plaintiff,

vs.

UNITED STATES OF AMERICA, JANE DOE,  
JOHN DOE, RICHARD BLACK, RICHARD  
ROE COMPANY, JIM GREEN COMPANY,  
JOHN DOE and RICHARD ROE, a Co-  
Partnership,

Defendants.

COMPLAINT TO QUIET TITLE  
TO PERSONAL PROPERTY

(Pursuant to 28 USC 2410)

Comes now All American Airways, Inc., a cor-  
poration, plaintiff herein, and for cause of action  
against the defendants and each of them, alleges:

I.

Plaintiff is a corporation organized under the  
laws of the State of Delaware.

II.

This action is instituted against the defendant  
United States of American under and pursuant to  
the provisions of Title 28 USC, Sec. 2410. United

States of America will hereinafter be referred to as the defendant. The purpose of this action is to quiet title in plaintiff and to secure an adjudication as to a lien [2] claimed by the defendant against the personal property hereinafter described, owned by plaintiff.

### III.

The defendants Jane Doe, John Doe, Richard Black, Richard Roe Company, Jim Green Company, John Doe & Richard Roe, a co-partnership, are sued herein under fictitious names, their true names being unknown to plaintiff. Upon ascertainment of said true names plaintiff will ask leave of Court to amend its complaint accordingly. Said defendants may claim some interest in and to the personal property hereinafter described.

### IV.

Plaintiff is now and since the dates hereinafter designated has been owner of those certain airplanes described as follows:

1. One Douglas DC-3, No. NC54312, purchased May 19, 1948;
2. One Douglas DC-3, No. NC49277, purchased May 19, 1948;
3. One Douglas DC-3, No. NC16839, purchased June 15, 1948.

Each of the above described airplanes is now in the plant of Douglas Aircraft, at Santa Monica, California, for purpose of overhaul and modification.



## V.

The above described airplanes are civil aircraft subject to the provisions of the Civil Aeronautics Act (Act of June 23, 1938, C601, 52 Stat. 977, 49 USC 401, et seq., as amended) and subject to the provisions of Section 503 of said Act (49 USCA Sec. 523), which statute provides for a system of recording all conveyances affecting the title to or interest in any civil aircraft of the United States. Prior to and at the time of purchasing the airplanes above specifically described plaintiff inspected the records of the Civil Aeronautics Board, Civil Aeronautics Administration, and Civil Aeronautics Authority in the Department of Commerce of the United States, all of which for convenience will be hereinafter referred to as [3] Civil Aeronautics Board, concerning the registration of aircraft and recordation of aircraft ownership and said Board's record with respect to the title and status of title and ownership of the above described airplanes. On and prior to June 15, 1948, there was no record of any claim or notice of lien or claim by defendant of any interest or lien in and to any of said airplanes, with the Civil Aeronautics Board.

## VI.

Plaintiff on and prior to June 15, 1948 had no notice that defendant claimed any lien or interest of any kind in and to any of said airplanes. For a good and valuable consideration and in good faith and without notice of any claim or interest of de-

fendant, plaintiff purchased said airplanes above described.

### VII.

On April 8, 1948, said airplanes were owned Northern Airlines, Inc., and defendant has informed plaintiff and on such information plaintiff alleges that said airplanes were, on April 8, 1948, physically in the City of Seattle, Kings County, State of Washington, the corporate domicile of Northern Airlines, Inc.

### VIII.

The defendant has furnished plaintiff the following information and on such information plaintiff alleges that the Commissioner of Internal Revenue assessed withholding taxes for the fourth quarter of the taxable year 1947 against Northern Airlines, Inc., in the sum of \$6,340.58, together with a penalty of \$634.06 and interest of \$60.88, or an aggregate sum of \$7,035.52, on or about the first day of April, 1948, and the Commissioner's assessment list carrying said tax was received in the office of the Collector of Internal Revenue at Tacoma, Washington, on the first day of April, 1948. The Commissioner of Internal Revenue assessed Federal insurance contributions taxes against Northern Airlines, [4] Inc., for the fourth quarter of the year 1947 in the sum of \$760.04, together with a penalty thereon of \$76.00 and interest of \$7.30, or an aggregate sum of \$843.36, on or about the first day of April, 1948, and the Commissioner's assessment list carrying

said tax was received in the Office of the Collector of Internal Revenue at Tacoma, Washington, on the fifth day of April, 1948. The Commissioner of Internal Revenue assessed Federal unemployment taxes for the year 1946 against Northern Airlines, Inc., in the sum of \$727.03, together with a penalty of \$36.35 and interest of \$50.60, or an aggregate assessment of \$813.98, on or about the first day of April, 1948, and the Commissioner's assessment list carrying said tax was received in the office of the Collector of Internal Revenue at Tacoma, Washington, on April 5, 1948. The Commissioner of Internal Revenue assessed transportation of property tax against Northern Airlines, Inc., for the period from October, 1947, through January, 1948, both months inclusive, in the sum of \$18,812.27, together with a penalty of \$2,764.16 and interest of \$278.53, or an aggregate assessment of transportation of property taxes, penalty and interest of \$21,854.96, on or about April 3, 1948. The Commissioner of Internal Revenue's assessment list carrying said transportation of property tax was received in the office of the Collector of Internal Revenue at Tacoma, Washington, on April 7, 1948. That upon receipt of said Commissioner of Internal Revenue's assessment list, the Collector of Internal Revenue at Tacoma, Washington, issued notice and demand for the payment of said taxes, penalties, and interest assessed as aforesaid, but no part of the same has been paid and the whole thereof remains assessed and unpaid. That thereafter and

on the eighth day of April, 1948, the Collector of Internal Revenue filed a notice of Federal tax lien in the office of the Auditor of King County, State of Washington, and on the thirteenth of April, 1948, he filed a like notice in the office of the Clerk of the United States District Court for the Western District of the State of Washington, [5] a copy of said notice of lien is hereto attached and marked Exhibit A.

### IX.

However, on and prior to June 15, 1948, defendant had not caused to be recorded any notice of such lien with the Civil Aeronautics Board in accordance with the provisions of Sec. 503 of Civil Aeronautics Act (49 USCA 523). Plaintiff at the time it purchased the airplanes as above alleged, had no notice of said claimed tax lien or that Northern Airlines, Inc., owed defendant any unpaid taxes or any money.

### X.

On September 2, 1948, defendant caused to be filed with Douglas Aircraft at Santa Monica, a levy of lien on said three airplanes.

### XI.

By reason of the foregoing, defendant claims and asserts some right, title, lien or interest in and to said personal property adverse to plaintiff. Defendant has no estate, right, title, interest or lien in and to said airplanes or any of them.

Wherefore, plaintiff prays that defendants and

each of them be required to set forth the nature of their respective claims and that all adverse claims of said defendants be determined by decree of this court; and that by said decree it be declared that none of the defendants has any estate, right, title, interest or lien whatever in and to said airplanes or any of said airplanes adverse to plaintiff, and that defendants and each of them be debarred forever from asserting any claim whatever in and to any of said airplanes; that judgment be entered in favor of plaintiff, that it recover its costs of suit, and have such other relief as the court may deem meet and equitable.

Dated: Los Angeles, California, November 9, 1948.

GUTHRIE, DARLING &  
SHATTUCK,

By /s/ MILO V. OLSON,  
Attorneys for Plaintiff. [6]

EXHIBIT A

Copy

Notice of Tax Lien(s) Under Internal  
Revenue Laws  
No. 11783

United States Internal Revenue,  
District of Washington,

April 7, 1948.

Pursuant to the provisions of Sections 3670, 3671, and 3672 of the Internal Revenue Code of the United States, notice is hereby given that there



have been assessed under the Internal Revenue laws of the United States against the following-named taxpayer, taxes (including interest and penalties) which after demand for payment thereof remain unpaid, and that by virtue of the above-mentioned statutes the amount (or amounts) of said taxes, together with penalties, interest, and costs that may accrue in addition thereto, is (or are) a lien (or liens) in favor of the United States upon all property and rights to property belonging to said taxpayer, to wit:

Name of taxpayer, Northen Airlines, Inc.

Residence or place of business, Boeing Field, Seattle, Washington.

Nature of Tax	Year or Taxable Period Ended	Date Assessment List Received	Amount of Assessment	
Withholding Tax Employment	Qtr. 12-31-47	4/1/48	T	6340.58
			P	634.06
			I	60.88
Tax—FICA	Qtr. 12-31-47	4/5/48	T	760.04
			P	76.00
			I	7.30
Employment Tax—FUTA	Year 1946 Suppl.	4/5/48	T	727.03
			P	36.35
			I	50.60
Trans. Prop. Tax	Oct '47 thru Jan '48	4/7/48	T	18812.27
			P	2764.16
			I	278.53
Filing Fee				.50
Total				30548.30

I hereby certify that this is a true copy of Lien #11783 for Northern Airlines, Inc., Boeing Field, Seattle, Washington, prepared on April 7, 1948.

/s/ CLARK SQUIRE.

Subscribed and sworn to before me this 30th day of August, 1948.

[Seal]                      MARGARET C. JOSSELYN  
Collector.

Certificate of Officer Authorized by Law to Take Acknowledgments.

Notary Public in and for the State of Washington,  
residing at Tacoma, Washington.

State of Washington,  
County of Pierce—ss.

Before me, this day personally appeared Clark Squire, to me well known, and well known by me to be the person described in and who executed the foregoing instrument as Collector of Internal Revenue for the ..... Collection District of Washington; and he acknowledged before me that he executed the same as such Collector of Internal Revenue, and for the purpose herein expressed.

Witness my hand and official seal at Tacoma, Washington, in the County and State aforesaid, this 7th day of April, 1948.

[Seal]        /s/ S. J. KALIVAS,  
Notary Public.

2 Copies—Auditor of King County.

(Filed 4/8/48 #2297356)

2 Copies—Clerk of U.S. Dist. Court.

(Filed 4/13/48.)

Affidavit of Service by of mail attached. •

[Endorsed]: Filed Nov. 10, 1948. [7]

[Title of District Court and Cause.]

MOTION TO DISMISS

Comes Now the United States of America, defendant herein, and moves the Court as follows:

(1) To dismiss the action because the complaint fails to state a claim against defendant upon which relief can be granted. This motion is based upon the files and pleadings in the case, a memorandum of points and authorities in support of the motion being filed by defendant concurrently herewith.

Dated: This 14th day of January, 1949.

JAMES M. CARTER,

United States Attorney.

E. H. MITCHELL,

Assistant U. S. Attorney.

EUGENE HARPOLE and

ROBERT D. SCOTT,

Special Attorneys, Bureau of  
Internal Revenue.

By /s/ EUGENE HARPOLE,

Attorneys for Defendant

United States of America.

Affidavit of Service by mail attached.

[Endorsed]: Filed Jan. 14, 1949. [8]

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At a stated term, to wit: The February Term, A.D. 1949, of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the

Court Room thereof, in the City of Los Angeles on Monday, the 16th day of May, in the year of our Lord one thousand nine hundred and forty-nine.

Present: The Honorable Jacob Weinberger,  
District Judge.

[Title of Cause.]

For further hearing motion of defendant, filed Jan. 14, 1949, to dismiss the action because the complaint fails to state a claim against defendant upon which relief can be granted; M. V. Olson, Esq., appearing as counsel for plaintiff; R. D. Scott, Spec. Att'y, Bureau of Internal Revenue, appearing as counsel for Gov't; Court orders said motion denied without prejudice, defendant to have twenty days to answer complaint. [10]

---

[Title of District Court and Cause.]

### NOTICE OF RULING

To the Defendant United States of America, and  
to James M. Carter, E. H. Mitchell, Eugene  
Harpole, Robert D. Scott and James D. Pettus,  
Its Attorneys:

You and Each of You Will Please Take Notice that on Monday, May 16, 1949, in the above-entitled matter, the Court, by the Honorable Jacob Weinberger, United States District Judge for the Southern District of California, by an order duly given and made, denied without prejudice the motion of

defendant United States of America to dismiss the action, and by said order the court granted defendant twenty days within which to answer the plaintiff's complaint on file herein.

Dated: May 16, 1949.

GUTHRIE, DARLING &  
SHATTUCK,

By /s/ MILO V. OLSON,  
Attorneys for Plaintiff.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed May 17, 1949. [11]

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[Title of District Court and Cause.]

### STIPULATION

It Is Stipulated between plaintiff and defendant United States of America through their attorneys of record:

1. That defendant United States of America will not file an answer or other or further pleading to plaintiff's complaint.

2. That the action may be dismissed as to all fictitiously named defendants.

3. That plaintiff may apply forthwith for judgment in the form attached hereto marked Exhibit A and that the judgment may be signed and entered by the court *ex parte* and without service of a three-day written notice as provided by Rule 55 (b) (2), Federal Rules of Civil Procedure.



4. That the judgment may be signed and entered on the allegations in plaintiff's complaint without supporting evidence [13] and without other or further compliance with rule 55(e), Federal Rules of Civil Procedure.

Dated: June 3rd, 1949.

JAMES M. CARTER,

United States Attorney.

E. H. MITCHELL,

Assistant U. S. Attorney.

EUGENE HARPOLE and

ROBERT D. SCOTT,

Special Attorneys, Bureau of  
Internal Revenue.

By /s/ EUGENE HARPOLE,

Attorneys for Defendant,

United States of America.

GUTHRIE, DARLING &

SHATTUCK,

By /s/ MILO V. OLSON,

Attorneys for Plaintiff.

[Endorsed]: Filed June 7, 1949.

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[Title of District Court and Cause.]

### JUDGMENT

The motion of defendant United States of America to dismiss the above-entitled action having been argued, heard and denied on May 16, 1949, and plaintiff and defendant United States of America having stipulated in the record of the above-entitled

proceeding that no answer or further pleading to plaintiff's complaint will be filed by defendant United States of America, and the court having been fully advised and good cause therefor appearing,

It Is Found, Ordered, Adjudged and Decreed:

1. That this Court has jurisdiction of the cause of action set forth in plaintiff's complaint.

2. That all of the allegations in plaintiff's complaint are true, except the allegations in Paragraph III thereof which are found to be immaterial.

3. That plaintiff is the owner of the following described [18] airplanes which are the subject matter of the within action:

One Douglas DC-3, No. NC54312, purchased May 19, 1948;

One Douglas DC-3, No. NC49277, purchased May 19, 1948;

One Douglas DC-3, No. NC16839, purchased June 15, 1948.

4. That the action be and it is dismissed as against the fictitiously named defendants.

5. That plaintiff is a bona fide purchaser of the airplanes described in Paragraph 3 of this judgment without notice of any claim of defendant, United States of America, in and to any of said airplanes because of the failure of defendant, United States of America, to record any notice or claim of its tax lien or liens against Northern Airlines, Inc., with the Civil Aeronautics Board

or the administrator of the Civil Aeronautics Board in accordance with the provisions of the Civil Aeronautics Act prior to the time plaintiff acquired ownership of said airplanes.

6. That defendant United States of America has no estate, right, title, interest or lien in or to any of the airplanes described in Paragraph 3 of this judgment, prior, superior or adverse to the estate, right, title and interest of plaintiff.

7. That defendant United States of America and all persons, firms, corporations and bodies politic acting under or through defendant United States of America be and they are forever barred and enjoined from asserting any claim in or to any of the airplanes described in Paragraph 3 of this judgment as against plaintiff's interest and ownership therein, by reason of or arising out of any unpaid taxes owing or claimed to be owed by Northern Airlines, Inc., to defendant United States of America.

8. That plaintiff's right, title, interest and possession in and to the airplanes described in Paragraph 3 of this judgment be and they are quieted against any right, title, interest, lien or claim of defendant United States of America or any person, firm, corporation or body politic acting under or through defendant United States of America.

Dated: June 7, 1949.

/s/ JACOB WEINBERGER,  
U. S. District Judge.

[Endorsed]: Filed June 7, 1949. [19]

[Title of District Court and Cause.]

WRITTEN NOTICE OF ENTRY OF  
JUDGMENT

To the Defendant United States of America, and  
to James M. Carter, E. H. Mitchell, Eugene  
Harpole, Robert D. Scott and James D. Pettus,  
Its Attorneys:

You and Each of You Will Please Take Notice  
that on Tuesday, June 7, 1949, in the above-entitled  
action, in Judgment Book 58, Page 658, judgment  
was duly entered, said judgment is in favor of the  
plaintiff and against the defendant, United States  
of America.

Dated: June 10th, 1949.

GUTHRIE, DARLING &  
SHATTUCK,

By /s/ MILO V. OLSON,  
Attorneys for Plaintiff.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed June 10, 1949. [20]

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[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice Is Hereby Given That the United States  
of America, defendant herein, hereby appeals to  
the United States Court of Appeals for the Ninth  
Circuit from the final judgment entered herein by  
this Court on June 7, 1949.

Dated: This 1st day of August, 1949.

JAMES M. CARTER,  
United States Attorney.

E. H. MITCHELL and  
EDWARD R. McHALE,  
Assistant U. S. Attorneys.

EUGENE HARPOLE,  
ROBERT D. SCOTT and  
JAMES D. PETTUS,  
Special Attorneys.

By /s/ EUGENE HARPOLE,  
Attorneys for Defendant,  
United States of America.

[Endorsed]: Filed Aug. 1, 1949. [22]

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[Title of District Court and Cause.]

APPELLANT'S DESIGNATION OF CON-  
TENTS OF RECORD ON APPEAL

Comes Now the United States of America, Defendant and appellant herein, and hereby designates that the complete record consisting of the following be included in and contained in the record on appeal in the above-entitled cause:

1. Complaint.
2. Motion to Dismiss dated January 14, 1949.
3. Notice of Ruling dated May 16, 1949.
4. Stipulation dated June 3, 1949.
5. Judgment entered June 7, 1949.



6. Written Notice of Entry of Judgment dated June 10, 1949.

7. Notice of Appeal. [23]

8. This Designation.

9. Clerk's Certificate.

Dated: This 18th day of August, 1949.

JAMES M. CARTER,

United States Attorney.

E. H. MITCHELL and

EDWARD R. McHALE,

Assistant U. S. Attorneys.

EUGENE HARPOLE,

ROBERT D. SCOTT and

JAMES D. PETTUS,

Special Attorneys, Bureau of  
Internal Revenue.

By /s/ EUGENE HARPOLE,

Attorneys for Defendant,

United States of America.

### STIPULATION

It Is Hereby Stipulated for and on behalf of All American Airways, Inc., plaintiff and appellee herein, that the foregoing items, as designated by appellant, shall be included in and constitute the record on appeal in the above-entitled cause.

Dated: This 15th day of August, 1949.

GUTHRIE, DARLING &

SHATTUCK,

By /s/ MILO V. OLSON,

Attorneys for Plaintiff.

[Endorsed]: Filed Aug. 18, 1949.

[Title of District Court and Cause.]

### CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the United States District Court for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 24, inclusive, contain the original Complaint to Quiet Title to Personal Property; Motion to Dismiss; Notice of Ruling; Stipulation; Judgment; Written Notice of Entry of Judgment; Notice of Appeal; Designation of Contents of Record on Appeal and a full, true and correct copy of Minute Order Entered May 16, 1949, which constitute the record on appeal to the United States Court of Appeals for the Ninth Circuit.

Witness my hand and the seal of said District Court this 7th day of Sept., A.D. 1949.

EDMUND L. SMITH,  
Clerk.

[Seal] By /s/ THEODORE HOCKE,  
Chief Deputy.

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[Endorsed]: No. 12347. United States Court of Appeals for the Ninth Circuit. United States of America, Appellant, vs. All American Airways, Inc., Appellee. Transcript of Record. Appeal from the United States District Court for the Southern District of California, Central Division.

Filed September 9, 1949.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the  
Ninth Circuit.

In the United States Court of Appeals  
for the Ninth Circuit

Undocketed

UNITED STATES OF AMERICA,

Appellant,

vs.

ALL AMERICAN AIRWAYS, INC.,

a corporation,

Appellee.

APPELLANT'S STATEMENT OF POINTS  
TO BE RELIED UPON ON APPEAL

Pursuant to the provisions of Rule 19(6) of the Rules of Practice of the United States Court of Appeals for the Ninth Circuit, Appellant hereby designates the following points upon which it intends to rely in its appeal in the above entitled case:

1. The District Court erred in denying appellant's Motion to Dismiss.
2. The District Court erred in finding and concluding that plaintiff-appellee is a bona fide purchaser of the airplanes involved herein without notice of the claim of the United States because of the failure of the United States to record notice or claim of its lien or liens for taxes against Northern Airlines, Inc., with the Civil Aeronautics Board or the administrator of the Civil Aeronautics Board in accordance with the provisions of the Civil Aeronautics

Act prior to the time plaintiff acquired ownership of said airplanes.

3. The District Court erred in holding that the United States has no lien prior, superior or adverse to the estate, right, title and interest of the plaintiff-appellee, in or to any of the airplanes involved herein.
4. The District Court erred in failing to hold that the United States acquired tax liens upon the airplanes involved herein by virtue of the provisions of Section 3670 of the Internal Revenue Code, and that such liens, pursuant to Section 3672 of the Internal Revenue Code and the laws of the State of Washington, are by virtue of the recordation of notice thereof in the office of the Auditor of King County, State of Washington, prior to the time plaintiff-appellee acquired ownership, valid against the plaintiff-appellee, a subsequent purchaser.
5. The District Court erred in enjoining the United States from asserting a claim in or to the airplanes involved herein as against plaintiff-appellee's interest and ownership therein by reason of or arising out of unpaid taxes owed by Northern Airlines, Inc., to the United States.
6. The District Court erred in decreeing that plaintiff-appellee's right, title, interest and possession in and to the airplanes involved herein are quieted against any right, title, interest, lien or claim of the United States.

Dated: This 1st day of September, 1949.

JAMES M. CARTER,  
United States Attorney,  
E. H. MITCHELL and  
EDWARD R. McHALE,  
Assistant U. S. Attorneys,  
EUGENE HARPOLE,  
ROBERT D. SCOTT and  
JAMES D. PETTUS,  
Special Attorneys, Bureau of  
Internal Revenue.

By /s/ ROBERT D. SCOTT,  
Attorneys for Appellant,  
United States of America.

Received copy of the within Appellant's Statement of Points to be Relied Upon on Appeal this 1 day of September, 1949.

GUTHRIE, DARLING &  
SHATTUCK,

By: /s/ EDWARD SHATTUCK,  
Attorneys for Appellee.

[Endorsed]: Filed U.S.C.A. Sept. 9, 1949.

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[Title of Court of Appeals and Cause.]

APPELLANT'S DESIGNATION OF PARTS OF  
RECORD BELIEVED NECESSARY FOR  
CONSIDERATION ON APPEAL AND TO  
BE PRINTED.

Pursuant to Rule 19(6) of this Court, Appellant hereby designates the following parts of the record



which appellant believes necessary for consideration of the points upon which it intends to rely in this appeal, and which appellant desires to be printed:

1. Page 1, Names and addresses of attorneys.
2. Pages 2 to 7, Complaint, omitting title of court and cause and excerpts from Internal Revenue Code on the reverse of page 7.
3. Page 8, Motion to Dismiss omitting title of court and cause.
4. Page 10, Order Denying Defendant's Motion to Dismiss. [32]
5. Page 11, Notice of Ruling, omitting title of court and cause.
6. Pages 13 and 14, Stipulation, omitting title of court and cause.
7. Pages 18 and 19, Judgment, omitting title of court and cause.
8. Page 20, Written Notice of Entry of Judgment, omitting title of court and cause.
9. Page 22, Notice of Appeal, omitting title of court and cause.
10. Pages 23 and 24, Appellant's Designation of Contents of Record on Appeal, omitting title of court and cause.
11. Certificate of Clerk.
12. Appellant's Statement of Points to be Relied Upon on Appeal, captioned "In the United States Court of Appeals for the Ninth Circuit" and filed concurrently with this Designation.
13. This Designation.

Dated: This 1st day of September, 1949.

JAMES M. CARTER,  
United States Attorney.

E. H. MITCHELL and  
EDWARD R. McHALE,  
Assistant United States  
Attorneys. [33]

EUGENE HARPOLE,  
ROBERT D. SCOTT and  
JAMES D. PETTUS,  
Special Attorneys, Bureau  
of Internal Revenue.

By /s/ ROBERT D. SCOTT,  
Attorneys for Appellant,  
United States of America.

Received copy of the within Appellant's Designation of Parts of Record Believed Necessary for Consideration on Appeal and to be Printed this 1 day of September, 1949.

GUTHRIE, DARLING &  
SHATTUCK,

By /s/ EDWARD SHATTUCK,  
Attorneys for Appellee.

[Endorsed]: Filed U.S.C.A. Sept. 9, 1949. [34]



No. 12347

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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UNITED STATES OF AMERICA,

*Appellant,*

*vs.*

ALL AMERICA AIRWAYS, INC.,

*Appellee.*

---

Appeal from the United States District Court for the  
Southern District of California  
Central Division

---

## BRIEF FOR THE UNITED STATES.

---

THERON LAMAR CAUDLE,  
*Assistant Attorney General,*

ELLIS N. SLACK,

HARRY MARSELLI,  
*Special Assistants to the  
Attorney General.*

ERNEST A. TOLIN,  
*United States Attorney,*

E. H. MITCHELL,  
*Assistant United States Attorney,*  
600 Federal Building, Los Angeles 12,  
*Of Counsel.*

FILED

NOV 14 1961

U.S. DISTRICT COURT





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No. 12347

IN THE  
**United States Court of Appeals**  
FOR THE NINTH CIRCUIT

---

UNITED STATES OF AMERICA,

*Appellant,*

*vs.*

ALL AMERICA AIRWAYS, INC.,

*Appellee.*

---

**BRIEF FOR THE UNITED STATES.**

---

**Opinion Below.**

The District Court wrote no opinion.

**Jurisdiction.**

This is an action brought [R. 2-10] in the United States District Court for the Southern District of California, Central Division, by All American Airways, Inc., a corporation organized under the laws of the State of Delaware [R. 2] (hereinafter referred to as the "appellee"), against the United States<sup>1</sup> under 28 U. S. C., Section 2410 (Appendix, *infra*), to quiet title to three airplanes

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<sup>1</sup>Some fictitiously named persons were also joined as defendants [R. 2, 3], but the action as to them was dismissed [R. 15].



which were located in Santa Monica, California, at the time of the institution of the action [R. 3] on November 10, 1948 [R. 10], and against which the United States had asserted liens for unpaid taxes due from Northern Airlines, Inc. [R. 3, 5-7, 8-10].

On June 7, 1949, the District Court entered a judgment in favor of the appellee and against the United States [R. 14-16], from which this appeal was taken by notice of appeal filed on August 1, 1949 [R. 17-18], which was within less than the 60 days from the entry of judgment prescribed by 28 U. S. C., Section 2107, and Rule 73(a) of the Federal Rules of Civil Procedure, as amended, for the taking of an appeal in a case in which the United States is a party. Jurisdiction of this Court is conferred under 28 U. S. C., Section 1291.

### **Question Presented.**

Whether the Government's otherwise valid lien for unpaid federal taxes, under Section 3670 of the Internal Revenue Code, notice of which has been filed pursuant to Section 3672(a) of the Code, is invalid with respect to airplanes against a subsequent purchaser unless the tax lien has also been "recorded" with the Administrator of Civil Aeronautics.

### **Statutes and Regulations Involved.**

The pertinent provisions of the statutes and regulations are set forth in the Appendix, *infra*.

### Statement.

This is an action brought by the appellee under the provisions of 28 U. S. C., Section 2410, against the United States for the purpose of quieting title in appellee and of securing an adjudication as to a lien asserted by the United States against certain personal property alleged to be owned by the appellee [R. 2-3]. The allegations of the complaint [R. 2-10] may be stated as follows:

The appellee alleged that, at the time of the institution of the action (November 10, 1948 [R. 10]), it was the owner of three Douglas DC-3 airplanes which were then located in the plant of Douglas Aircraft, at Santa Monica, California, for the purpose of overhaul and modification; that it had purchased two of the planes on May 19, 1948, and the third on June 15, 1948, and that it had been the owner of them since those dates, respectively [R. 3].

The appellee further alleged that the three airplanes in question were civil aircraft subject to the provisions of the Civil Aeronautics Act of 1938, which provides for a system of recording of conveyances affecting title to, or interest in, any civil aircraft of the United States; that prior to and at the time of purchasing the airplanes in question, the appellee had inspected the records of the Civil Aeronautics Board concerning the registration of aircraft and recordation of aircraft ownership, and had inspected that Board's record with respect to the title and status of title and ownership of the three airplanes in question; and that on and prior to June 15, 1948, there was no record of any claim or notice of lien or claim by the United

States of any interest or lien in or to any of the three airplanes with the Civil Aeronautics Board [R. 4].

The appellee further alleged that on and prior to June 15, 1948, it had no notice that the United States claimed any lien or interest in any of the three airplanes in question, and that it had purchased the airplanes, for a good and valuable consideration, in good faith and without notice of any claim or interest of the United States [R. 4-5].

Appellee further alleged that the airplanes in question on April 8, 1948, were owned by Northern Airlines, Inc., and on that date were physically in the City of Seattle, King County, State of Washington, the corporate domicile of Northern Airlines, Inc. [R. 5].

The appellee further alleged that the Commissioner of Internal Revenue had assessed against Northern Airlines, Inc., certain withholding taxes, federal insurance contributions taxes, unemployment taxes, and taxes on transportation of property, with certain penalties and interest thereon,<sup>2</sup> and that the Commissioner's assessment lists carrying the assessments had been received in the office of the Collector of Internal Revenue at Tacoma, Washington, on April 1, 5, and 7, 1948; that upon receipt of these assessment lists the Collector of Internal Revenue at Tacoma had issued notice and demand for payment of the taxes, penalties, and interest in question, but no part thereof had been paid and the whole thereof remained assessed

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<sup>2</sup>In the complaint, the respective periods covered by the assessments of the several taxes, and the respective amounts assessed as tax, penalty, and interest as to each of the several taxes, were set forth in detail [R. 5-6], and in the copy of the notice of tax lien attached to the complaint, the respective amounts of taxes, penalties, and interest covered by the assessments were listed in a table showing the total thereof as amounting to \$30,548.30 [R. 9].

and unpaid; and that thereafter the Collector had filed notices of federal tax lien (a copy of which was attached to the complaint as Exhibit A, R. 8-10), on April 8, 1948, in the office of the Auditor of King County, of the State of Washington, and on April 13, 1948, in the office of the Clerk of the United States District Court for the Western District of the State of Washington [R. 5-7].

The complaint further alleged that on and prior to June 15, 1948, the United States had not caused any notice of that tax lien to be recorded with the Civil Aeronautics Board, in accordance with the provisions of Section 503 of the Civil Aeronautics Act; and that the appellee, at the time it purchased the airplanes, had no notice of the asserted tax lien or that Northern Airlines, Inc., owed the United States any unpaid taxes or any money [R. 7].

The appellee further alleged that on September 2, 1948, the United States had caused to be filed with Douglas Aircraft, at Santa Monica, a levy of lien on the three airplanes in question [R. 7].

The appellee further alleged that the United States was claiming and asserting some right, title, lien or interest in and to the personal property in question adverse to the appellee, and the appellee alleged that the United States had no estate, right, title, interest or lien in and to any of the three airplanes [R. 7].

The appellee in its complaint also joined as defendants certain fictitious persons who, it alleged, may claim some interest in the three airplanes in question [R. 3].

Upon the basis of the foregoing allegations, the appellee in its complaint prayed [R. 7-8] that the defendants be required to set forth the nature of their respective claims and that all adverse claims of the defendants be determined



in the action; and that the court decree that none of the defendants has any estate, right, title, interest or lien in and to any of the airplanes; and that judgment be entered in favor of the appellee, with costs, etc.

Thereafter, on January 14, 1949, the United States filed a "Motion to Dismiss" in which it moved the court to dismiss the action because the complaint failed to state a claim against the United States upon which relief could be granted [R. 11]. After hearing thereon, the District Court denied the motion without prejudice, on May 16, 1949, and allowed the United States 20 days within which to answer [R. 11-12].

Thereafter, instead of the United States filing an answer, counsel for the United States and the appellee entered into a stipulation on June 3, 1949, which was filed with the court below on June 7, 1949 [R. 14]. In that stipulation, it was agreed that the United States would not file an answer or further pleading, that the action be dismissed as to the fictitiously named defendants, and that the appellee could apply for judgment (in the form set forth in a draft of judgment submitted with the stipulation), and that the judgment could be signed and entered by the court, *ex parte*, without the service of a three-day notice as provided by Rule 55(b)(2) of the Federal Rules of Civil Procedure, and without the submission of supporting evidence required by Rule 55(e) of those rules [R. 13, 14].

Thereupon, the court below entered its judgment on June 7, 1949 [R. 14-16], wherein it decreed as follows:



That it had jurisdiction of the action; that all of the allegations of the appellee's complaint were true (with the exception of the allegations in paragraph III, with respect to the fictitiously named defendants, which were found to be immaterial, and as to which defendants the cause was dismissed); that the appellee was the owner of the three airplanes in question, two of which were purchased on May 19, 1948, and one on June 15, 1948; that the appellee was a *bona fide* purchaser of the three airplanes without notice of any claim of the United States thereon, because of the failure of the United States to record any notice or claim of its tax lien against Northern Airlines, Inc., with the Civil Aeronautics Board or the Administrator of Civil Aeronautics, in accordance with the provisions of the Civil Aeronautics Act, prior to the time the appellee acquired ownership of the airplanes; that the United States has no estate, right, title, interest or lien in the three airplanes prior, superior, or adverse to the right, title and interest of the appellee; that the United States, and all persons acting under it, be forever barred from asserting any claim to the three airplanes by reason of any unpaid taxes owed by Northern Airlines, Inc., to the United States; and that the appellee's title to the three airplanes is quieted against any lien or claim of the United States, or any person acting under it.

From that judgment, the present appeal was taken by the United States [R. 17-18].

### Statement of Points to Be Urged.

In the present appeal, the United States urges and relies upon all of the points originally stated by it in this Court as the points upon which it intended to rely [R. 21-23].

Briefly stated, the points urged and relied upon are that the District Court erred:

1. In denying the United States' motion to dismiss;
2. In holding that the appellee is a *bona fide* purchaser of the three airplanes without notice of the claim of the United States, because of the failure of the United States to record notice or claim of its lien for taxes against Northern Airlines, Inc., with the Administrator of Civil Aeronautics prior to the time the appellee acquired ownership of the airplanes;
3. In holding that the United States has no lien prior or superior to the appellee's title to the three airplanes;
4. In failing to hold that the United States acquired tax liens upon the three airplanes under Section 3670 of the Internal Revenue Code, and that, by the recording of the notice of those liens in the office of the Auditor of King County, State of Washington, prior to the time the appellee acquired ownership, those liens are valid against the appellee, a subsequent purchaser, under the provisions of Section 3672 of the Code;
5. In enjoining the United States from asserting a claim to the three airplanes by reason of any unpaid taxes owed by Northern Airlines, Inc.; and
6. In decreeing that the appellee's title to the three airplanes is quieted against any claim or lien of the United States.

## Summary of Argument.

The undisputed facts of this case establish conclusively that the tax lien in favor of the United States, under Section 3670 of the Internal Revenue Code, on the three airplanes in question was, after the Collector had filed a notice of lien in the local recording office in accordance with Section 3672 of the Code and the applicable Washington statute, valid against the appellee, a subsequent purchaser.

The tax lien in favor of the United States under Section 3670 of the Code applies to all property of a delinquent taxpayer, and under Section 3672 of the Code the only condition to the validity of that lien against subsequent purchaser of the property of a delinquent taxpayer is the filing of a notice of the lien either in the local recording office or in the office of the clerk of the District Court in the locality where the property is located. The decision of the court below, in effect, superimposes upon the plain terms of the statute an additional condition to the effect that as to airplanes the lien will not be valid against subsequent purchasers unless notice thereof is also filed with the Administrator of Civil Aeronautics.

The court below was clearly in error in treating the plain terms of the provisions of the Internal Revenue Code as to tax liens as having been amended by the recordation provisions of the Civil Aeronautics Act.

## ARGUMENT.

The Government's Lien for Unpaid Federal Taxes Under Section 3670 of the Internal Revenue Code, Notice of Which Had Been Filed Pursuant to Section 3672(a) of the Code, Was Valid With Respect to Airplanes Against the Appellee, a Subsequent Purchaser, Even Though the Tax Lien Had Not Been Also Recorded With the Administrator of Civil Aeronautics.

It is submitted that, under the facts of this case, the United States had a valid tax lien on the airplanes in question, which lien was valid against the appellee, a purchaser of the airplanes at a date subsequent to the filing of the notice of the tax lien pursuant to law, and that the District Court therefore erred in denying the motion to dismiss and in entering a judgment in favor of the appellee and against the United States in this action. The appellee acquired two of the airplanes on May 19, 1948, and the third one on June 15, 1948. Prior thereto, the Commissioner of Internal Revenue, on April 1, and 3, 1948, had made assessments of several taxes, with interest and penalties, aggregating \$30,548.30 against Northern Airlines, Inc., and the assessment lists containing those assessments were received in the office of the Collector of Internal Revenue at Tacoma, Washington, on April 1, 5, and 7, 1948, respectively. Under Section 3670 of the Internal Revenue Code (Appendix, *infra*) the amount of those taxes, including interest and penalties, became "a lien in favor of the United States upon all property and rights to property, whether real or personal" belonging to the taxpayer, Northern Airlines, Inc., and by virtue of Section 3671 of the Internal Revenue Code that lien arose on the days the respective assessment lists were received in the office of the Collector. On those days, in April,



1948, the three airplanes in question were owned by Northern Airlines, Inc. After having issued notice and demand for the payment of the taxes, interest and penalties, and while they remained unpaid, on April 8, 1948, the Collector filed a notice of the tax lien in the office of the Auditor of King County, State of Washington, and on that date the three airplanes were physically located in the City of Seattle, King County, State of Washington, the corporate domicile of Northern Airlines, Inc. Upon the filing of that notice of lien with the County Auditor, pursuant to the provisions of Sections 11337-1 to 11337-5 of Remington's Revised Statutes of Washington, Annotated (1933) (Appendix, *infra*), the tax lien of the United States became valid against the appellee, a subsequent purchaser of the airplanes, by virtue of the provisions of Section 3672(a) of the Internal Revenue Code (Appendix, *infra*). These admitted facts establish conclusively, we submit, that the tax lien of the United States on the three airplanes in question was valid against the appellee, a subsequent purchaser, and that the District Court was clearly in error in denying the Government's motion to dismiss the appellee's action to quiet title and in rendering a judgment in favor of the appellee and against the United States.

The clear, unambiguous, unqualified, and unrestricted provisions of Sections 3670, 3671 and 3672 of the Internal Revenue Code establish beyond any doubt, we submit, that the tax lien of the United States on the three airplanes was valid against the appellee, a purchaser of the airplanes at a time subsequent to the filing of the notice of lien with the County Auditor, as authorized by the law of the State of Washington. Section 3670 of the Code creates a lien in favor of the United States "upon all property" of the delinquent taxpayer, and Sec-



tion 3671 makes that lien applicable from the time the assessment list is received by the Collector. Section 3672 of the Code makes that lien valid even against a purchaser of property of the delinquent taxpayer after a notice of the lien has been filed by the Collector in the recording office of the locality where the property is located. The judgment of the court below, we submit, is clearly contrary to the plain terms of these statutory provisions and is unquestionably erroneous. Under Section 3672(a)(1) and (2) of the Code, the only condition to the validity of the Government's tax lien against a subsequent purchaser of property of a delinquent taxpayer is the filing of a notice of the tax lien by the Collector either in the local recording office or in the office of the clerk of the District Court where the property is situated. The effect of the decision of the court below is to superimpose upon the terms of that statute a further condition or requirement to the effect that the tax lien will not be valid with respect to airplanes unless the Collector has also filed a notice thereof with the Administrator of Civil Aeronautics.

Obviously, what the court below did to arrive at its decision was to treat the aircraft ownership recordation provisions of Section 503 of the Civil Aeronautics Act of 1938 (Appendix, *infra*) as amending the provisions of Sections 3670, 3671 and 3672 of the Internal Revenue Code so as to provide that in order for tax lien to be effective as to airplanes they must also be recorded with the Administrator of Civil Aeronautics. The court below was clearly in error, we submit. It is a well established and fundamental rule of construction that a statute which in general terms divest pre-existing rights or privileges will not be applied against the sovereign without express words to that effect. See *United States v. Mine Workers*, 330 U. S. 258, 272. See also *California Iron Yards Co.*

*v. Commissioner*, 47 F. 2d 514 (C. A. 9th), and cases cited at p. 516; and *Liebes v. Commissioner*, 63 F. 2d 870, 872 (C. A. 9th). Section 503 of the Civil Aeronautics Act, which provides for recordation of aircraft ownership, obviously does not contain any express language relating to tax liens in favor of the United States, and therefore its general terms cannot be regarded as limiting or taking away the pre-existing rights of the United States with respect to tax liens under the Internal Revenue Code, without any express words to that effect.

Even without regard to that rule of construction, however, it is clear that Section 503 of the Civil Aeronautics Act does not apply to tax liens created under the Internal Revenue Code. Section 503 of the Civil Aeronautics Act provides, in substance, that no "conveyance" of aircraft shall be valid against a subsequent purchaser until filed for recordation with the Administrator of Civil Aeronautics. Section 1(18) of the Civil Aeronautics Act of 1938 (Appendix, *infra*) defines the term "conveyance" as meaning "a bill of sale, contract of conditional sale, mortgage, assignment of mortgage, or other instrument affecting title to, or interest in, property." Tax liens are not expressly included in that definition and they cannot, we submit, be regarded as being included in the general phrase "or other instrument affecting title to, or interest in, property." A tax lien arises not by "instrument" but by operation of law, *i. e.*, under Section 3670 of the Internal Revenue Code. A tax lien is not a "conveyance" in the usual, plain and ordinary meaning of that term, in which it must be assumed to have been used in the statute: *i. e.*, a tax lien is not a transfer made or given by one person to another of a right or an interest in property, even though the law under Section 3672 of the Code provides for the filing of a piece of paper or document so as

to make the tax lien effective as against subsequent purchasers, etc. All of the instruments specifically named in the statutory definition of "conveyance" are of the character used to effect a transfer by an owner of property of some interest or right therein, *by affirmative act*—hence, under the rule of *ejusdem generis*, the "other instrument" phrase should be construed as including only documents of the same general character and should not be extended to include a tax lien, which comes into being by operation of law and not by the owner's act. Moreover, the report of the House Committee on Interstate and Foreign Commerce, on the proposed provisions for the recordation of aircraft ownership, further supports the view that the term "conveyance" was used in the sense of a transfer from one person to another, and it fails to disclose any intention to include tax liens. (H. Rep. No. 2254, 75th Cong., 3d Sess., p. 9.)

Another consideration is appropriate in this connection. It has become settled that the Government's tax liens attach even to after-acquired property. (See *Citizens Nat. Trust & Sav. Bank of Los Angeles v. United States*, 135 F. 2d 527 (C. A. 9th); *Nelson v. United States*, 139 F. 2d 162 (C. A. 9th), certiorari denied, 322 U. S. 764; *Investment & Securities Co. v. United States*, 140 F. 2d 894 (C. A. 9th); *Glass City Bank v. United States*, 326 U. S. 265.) Therefore, if the decision below were correct, the Government, in order to protect its tax liens, would be forced to file them for recordation with the Administrator of Civil Aeronautics not only with respect to taxpayers engaged in the commercial airline business but also as to all individuals and corporate taxpayers, whatever their business, on the supposition that any of them may possibly later acquire an airplane. However, under Section 503 of the Civil Aeronautics Act and the regulations on recorda-

tion of aircraft ownership promulgated thereunder (14 Code of Federal Regulations, 1947 Supp., Part 503 and Part 651, Appendix, *infra*), Collectors' notices of tax liens would not be eligible for recordation with the Administrator of Civil Aeronautics, since the recordation of a "conveyance" which does not state the interest in the aircraft of the person by whom the conveyance is made, is prohibited. Those regulations clearly indicate that the Administrator of Civil Aeronautics has construed the term "conveyance" as used in Section 503(b) of the Civil Aeronautics Act as not including tax liens created under the Internal Revenue Code.

In the absence of specific provisions to the contrary, we submit, the provisions of Sections 3670, 3671 and 3672 of the Internal Revenue Code should be held to govern the validity of federal tax liens and to be unaffected by the provisions of the Civil Aeronautics Act. (*Cf. Illinois v. United States*, 328 U. S. 8.) There is nothing in the Civil Aeronautics Act which could possibly be regarded as even approaching an express declaration that the provisions for the recordation of aircraft ownership and of "conveyances" affecting title to or interest in civil aircraft included federal tax liens, nor is there any indication of a congressional purpose to include federal tax liens.

While there is nothing in the record to disclose the reasoning of the court below, it is reasonable to assume that it may have been influenced by considerations as to the implications behind the general scheme of the Civil Aeronautics Act to provide for a central place for the recordation of aircraft ownership and of conveyances affecting title to aircraft. It may also have been influenced by considerations to the effect that, if tax liens be held valid as to aircraft without being recorded with the Ad-



ministrator of Civil Aeronautics, that might weaken the effectiveness and reliability of the aircraft ownership recordation system and might frustrate the purpose of Congress in establishing the central recordation system. Or, perhaps, the court below might have been influenced by the thought that if a purchaser of aircraft, such as the appellee, could not rely on the Civil Aeronautics recording system as to tax liens, he might be subjected to an endless search of the records of every county in every state. Such thought would, of course, be erroneous, because all that the appellee had to do was to search the records of the county of domicile of the seller, *i. e.*, King County, Washington, and it would have ascertained the existence of a tax lien in favor of the United States. Obviously, the fact that the appellee did not do that and the further fact that, as alleged in its complaint [R. 7], at the time it purchased the airplanes, it had no notice of the Government's tax lien or of the fact that Northern Airlines, Inc., owed the Government any unpaid taxes, are wholly immaterial and of no significance. As has been aptly stated in *Equitable Life Assur. Soc. v. Moore*, 29 Fed. Supp. 179, 184 (E. D. Ill.), "parties dealing with the property of the taxpayer against whom a tax lien has been filed are charged with notice of the recorded lien \* \* \*. It was the intent of Congress to give notice to third parties by the filing of the lien" with either the local recording office or the clerk of the District Court, pursuant to Section 3672 of the Internal Revenue Code.

There is little merit to considerations such as those we have indicated may have influenced the court below, we submit. In any event, considerations or arguments such as those clearly should have no bearing and should be given no weight in the determination of the present controversy: They are really addressed to legislative policy,



in effect attacking the "wisdom" of the law as it is under the statute and in effect arguing as to what the law should be or as to what would be a "better" law. But it is well settled that the courts must not add to the provisions of a statute or supply an omission or question the wisdom of the legislative body in adopting certain provisions and not adopting others. (*Security-First Nat. Bank of Los Angeles v. Welch*, 92 F. 2d 357, 359-360 (C. A. 9th), certiorari denied, 303 U. S. 638. See also *Caminetti v. United States*, 242 U. S. 470; *Heiner v. Donnan*, 285 U. S. 312; and *Glass City Bank v. United States*, *supra*, p. 268.)

The important factor in this case is that the recordation provisions of the Civil Aeronautics Act does not expressly include tax liens created under the Internal Revenue Code. Whatever appeal there might be in considerations of the character we have said may have influenced the court below, they cannot possibly support the conclusion that in adopting the recordation provisions of the Civil Aeronautics Act Congress intended in effect to amend the provisions of Sections 3670, 3671 and 3672 of the Internal Revenue Code. (*Cf. Illinois v. United States*, *supra*.) Congress was well aware of those provisions of the Internal Revenue Code when it passed the Civil Aeronautics Act. If it had intended that the recordation provisions of that Act apply to tax liens with respect to civil aircraft, it would have said so specifically in that Act,<sup>3</sup> or it would

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<sup>3</sup>For example, when Congress wanted to subordinate tax liens to administration costs and wage claims in bankruptcy, it did so specifically by express provisions written into the Bankruptcy Act of 1898, c. 541, 30 Stat. 544, Sec. 67, as amended (11 U. S. C., 1946 ed., Sec. 107(c)).

have separately amended Section 3672 so as to provide for a further requirement that, in order to be effective with respect to aircraft, tax liens must also be recorded with the Administrator of Civil Aeronautics. But Congress did neither of those things. The provisions of the Civil Aeronautics Act which it adopted clearly do not amend, either directly or by necessary implication, the provisions of the Internal Revenue Code with respect to tax liens, Sections 3670, 3671 and 3672. Nor can the provisions of the Civil Aeronautics Act possibly be regarded as inconsistent with those provisions of the Internal Revenue Code. Indeed, what has been said by the Supreme Court, in a similar situation with regard to Section 3466 of the Revised Statutes establishing priority for debts due to the United States, may well be said here: "Only the plainest inconsistency would warrant \* \* \* finding an implied exception to the operation of so clear a command." (*United States v. Emory*, 314 U. S. 423, 433; and *Illinois v. United States*, *supra*, p. 12) as that of Section 3670 of the Internal Revenue Code. In speaking of the lien created by Section 3670 of the Code, the Supreme Court in the *Glass City Bank* case, p. 267, stated: "Stronger language could hardly have been selected to reveal a purpose to assure the collection of taxes." Section 3670 imposes a lien for unpaid taxes "upon all property and rights to property, whether real or personal" belonging to a delinquent taxpayer. That language, as already noted, is broad and unqualified and unrestricted. It was recognized long ago that the lien created by that statute is a "sweep-

ing lien" upon all property and rights to property belonging to the delinquent taxpayer. (See *Blacklock v. United States*, 208 U. S. 75.) This court has consistently recognized that the statute "is unambiguous and all-inclusive." (*MacKenzie v. United States*, 109 F. 2d 540, 542.)

It is submitted that the decision of the court below is unquestionably erroneous. The lien in favor of the United States, for the unpaid taxes due from the delinquent taxpayer, Northern Airlines, Inc., attached and was perfected and became valid on the three airplanes in question even against subsequent purchasers, such as the appellee, on April 8, 1948, upon the filing of the notice of lien with the county auditor. Upon its purchase of the airplanes in May and in June, 1948, the appellee unquestionably took title subject to the lien in favor of the United States. There can be no question, of course, as to the general proposition that a perfected lien, prior in point of time, prevails over rights created or arising subsequent thereto. (See *Michigan v. United States*, 317 U. S. 338; *cf. United States v. Sampsell*, 153 F. 2d 731 (C. A. 9th); and *Miller v. Bank of America N. T. & S. A.*, 166 F. 2d 415 (C. A. 9th).) Since the United States had a valid prior lien on the airplanes in question, the court below should have dismissed the appellee's action to quiet title to the airplanes in the appellee.

### Conclusion.

It is submitted that the judgment entered in the District Court should be reversed, with directions to enter a judgment dismissing the action.

Respectfully submitted,

THERON LAMAR CAUDLE,  
*Assistant Attorney General,*

ELLIS N. SLACK,

HARRY MARSELLI,  
*Special Assistants to the  
Attorney General.*

ERNEST A. TOLIN,  
*United States Attorney,*

E. H. MITCHELL,  
*Assistant United States Attorney,  
Of Counsel.*

November, 1949.







## APPENDIX.

28 U. S. C.:

§2410. *Actions affecting property on which United States has lien.*

(a) Under the conditions prescribed in this section and section 1444 of this title for the protection of the United States, the United States may be named a party in any civil action or suit in any district court, including the District Court for the Territory of Alaska, or in any State court having jurisdiction of the subject matter, to quiet title to or for the foreclosure of a mortgage or other lien upon real or personal property on which the United States has or claims a mortgage or other lien.

(b) The complaint shall set forth with particularity the nature of the interest or lien of the United States. The United States may appear and answer, plead or demur within sixty days after service, or such further times as the court may allow.

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Internal Revenue Code:

INTERNAL REVENUE TITLE.

\* \* \* \* \*

CHAPTER 35—ASSESSMENT.

SEC. 3640. ASSESSMENT AUTHORITY.

The Commissioner is authorized and required to make the inquiries, determinations, and assessments of all taxes and penalties imposed by this title, or accruing under any former internal revenue law, where such taxes have not been duly paid by stamp at the time and in the manner provided by law.

(26 U. S. C. 1946 ed., Sec. 3640.)

SEC. 3641. CERTIFICATION OF ASSESSMENT LISTS TO COLLECTORS.

The Commissioner shall certify a list of such assessments when made to the proper collectors, respectively, who shall proceed to collect and account for the taxes and penalties so certified.

(26 U. S. C. 1946 ed., Sec. 3641.)

CHAPTER 36—COLLECTION.

\* \* \* \* \*

SEC. 3651. COLLECTION AUTHORITY.

(a) *In General.*—

(1) *Within district.*—It shall be the duty of collectors or their deputies, in their respective districts, and they are authorized, to collect all the taxes imposed by law, however the same may be designated.

\* \* \* \* \*

(26 U. S. C. 1946 ed., Sec. 3651.)

SEC. 3655. NOTICE AND DEMAND FOR TAX.

(a) *Delivery.*—Where it is not otherwise provided, the collector shall in person or by deputy, within ten days after receiving any list of taxes from the Commissioner, give notice to each person liable to pay any taxes stated therein, to be left at his dwelling or usual place of business, or to be sent by mail, stating the amount of such taxes and demanding payment thereof.

\* \* \* \* \*

(26 U. S. C. 1946 ed., Sec. 3655.)

SUBCHAPTER B—LIEN FOR TAXES.

SEC. 3670. PROPERTY SUBJECT TO LIEN.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

(26 U. S. C. 1946 ed., Sec. 3670.)

SEC. 3671. PERIOD OF LIEN.

Unless another date is specifically fixed by law, the lien shall arise at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of times.

(26 U. S. C. 1946 ed., Sec. 3671.)

SEC. 3672 [as amended by Section 401 of the Revenue Act of 1939, c. 247, 53 Stat. 862, and Section 505 of the Revenue Act of 1942, c. 619, 56 Stat. 798].

VALIDITY AGAINST MORTGAGEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS.

(a) *Invalidity of Lien Without Notice.*—Such lien shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the collector—

(1) *Under state or territorial laws.*—In the office in which the filing of such notice is authorized

by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law authorized the filing of such notice in an office within the State or Territory; or

(2) *With clerk of district court.*—In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State or Territory has not by law authorized the filing of such notice in an office within the State or Territory; \* \* \*

\* \* \* \* \*

(26 U. S. C. 1946 ed., Sec. 3672.)

11 Remington's Revised Statutes of Washington, Annotated (1933):

# LIENS FOR UNITED STATES INTERNAL REVENUE TAX.

§11337-1. *Notice of lien may be filed.* Notices of liens for internal revenue taxes payable to the United States of America and certificates discharging such liens may be filed in the office of the county auditor of any county or counties of the state of Washington within which the property subject to such lien is situated.

§11337-2. *Notice to be entered by county auditor.* When a notice of such tax lien is filed, the county auditor shall forthwith enter the same in an alphabetical federal tax lien index to be provided by the board of county commissioners, showing on one line the name and residence of the taxpayer named in such notice, the collector's serial number of such notice, the date and hour of filing, and



the amount of tax and penalty assessed. He shall file and keep all original notices so filed in municipal order in a file or files to be provided by the board of county commissioners and designated federal tax lien notices.

§11337-3. *Certificate of discharge to be entered by county auditor.* When a certificate or discharge of any tax lien, issued by the collector of internal revenue or other proper officer, is filed in the office of the county auditor, where the original notice of lien is filed, said county auditor shall enter the same with date of filing in said tax lien index on a line where the notice of the lien so discharged is entered, and permanently attach the original certificate of discharge to the original notice of lien.

§11337-4. *Fee.* Said county auditor shall receive twenty-five cents for filing and indexing each notice of lien and each certificate of discharge.

§11337-5. *Purpose of act.* This act is passed for the purpose of authorizing the filing of notices of liens in accordance with the provisions of section 3186 of the Revised Statutes of the United States, as amended by the Act of March 4, 1913, 37 Statutes at Large, page 1016.<sup>1</sup>

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<sup>1</sup>The material portions of Section 3186 of the Revised Statutes became Section 3672 of the Internal Revenue Code.

Civil Aeronautics Act of 1938, c. 601, 52 Stat. 973:

TITLE I—GENERAL PROVISIONS.

*Definitions.*

Section 1. As used in this Act, unless the context otherwise requires—

\* \* \* \* \*

(4) "Aircraft" means any contrivance now known or hereafter invented, used, or designed for navigation of or flight in the air.

\* \* \* \* \*

(14) "Civil aircraft" means any aircraft other than a public aircraft.

(15) "Civil aircraft of the United States" means any aircraft registered as provided in this Act.

\* \* \* \* \*

(18) "Conveyance" means a bill of sale, contract of conditional sale, mortgage, assignment of mortgage, or other instrument affecting title to, or interest in, property.

\* \* \* \* \*

(49 U. S. C. 1946 ed., Sec. 401.)

TITLE V—NATIONALITY AND OWNERSHIP OF AIRCRAFT.

*Registration of aircraft nationality.<sup>2</sup>*

*Registration Required.*

Sec. 501. (a) It shall be unlawful for any person to operate or navigate any aircraft eligible for registration

---

<sup>2</sup>The functions of aircraft registration and ownership recordation were transferred to the Administrator of Civil Aeronautics by Reorganization Plans III and IV, 54 Stat. 1233 and 1235, effective June 30, 1940, as the result of which the title of the "Administrator of Civil Aeronautics" became substituted for the term "Authority" in the statute quoted above.

if such aircraft is not registered by its owner as provided in this section, or (except as provided in section 6 of the Air Commerce Act of 1926, as amended) to operate or navigate within the United States any aircraft not eligible for registration: *Provided*, That aircraft of the national defense forces of the United States may be operated and navigated without being so registered if such aircraft are identified, by the agency having jurisdiction over them, in a manner satisfactory to the Authority. The Authority may, by regulation, permit the operation and navigation of aircraft without registration by the owner for such reasonable periods after transfer of ownership thereof as the Authority may prescribe.

*Eligibility for Registration.*

(b) An aircraft shall be eligible for registration if, but only if—

(1) It is owned by a citizen of the United States and is not registered under the laws of any foreign country; or

\* \* \* \* \*

*Issuance of Certificate.*

(c) Upon request of the owner of any aircraft eligible for registration, such aircraft shall be registered by the Authority and the Authority shall issue to the owner thereof a certificate of registration.

\* \* \* \* \*

*Effect of Registration.*

(f) Such certificate shall be conclusive evidence of nationality for international purposes, but not in any proceeding under the laws of the United States. Registration shall not be evidence of ownership of aircraft in any

proceeding in which such ownership by a particular person is, or may be, in issue.

\* \* \* \* \*

(49 U. S. C. 1946 ed., Sec. 521.)

*Recordation of aircraft ownership.*

*Establishment of Recording System.*

Sec. 503. (a) The Authority shall establish and maintain a system for recording all conveyances affecting the title to, or interest in, any civil aircraft of the United States.

*Conveyances to be Recorded.*

(b) No conveyance made or given on or after the effective date of this section, which affects the title to, or interest in, any civil aircraft of the United States, or any portion thereof, shall be valid in respect of such aircraft or portion thereof against any person other than the person by whom the conveyance is made or given, his heir or devisee, and any person having actual notice thereof, until such conveyance is recorded in the office of the secretary of the Authority. Every such conveyance so recorded in the office of the secretary of the Authority shall be valid as to all persons without further recordation. Any instrument, recordation of which is required by the provisions of this section, shall take effect from the date of its recordation, and not from the date of its execution.

*Form of Conveyance.*

(c) No conveyance shall be recorded, unless it states the interest in the aircraft of the person by whom such conveyance is made or given or, in the case of a contract of conditional sale, the interest of the vendor, and states the



interest transferred by the conveyance, and unless it shall have been acknowledged before a notary public or other officer authorized by law of the United States, or of a State, Territory, or possession thereof, or the District of Columbia, to take acknowledgment of deeds.

### *Index of Conveyances.*

(d) The Authority shall record conveyances delivered to it in the order of their reception, in files to be kept for that purpose, and indexed to show—

- (1) the identifying description of the aircraft;
- (2) the names of the parties to the conveyance;
- (3) the time and date of reception of the instrument and the time and date of recordation thereof;
- (4) the interest in the aircraft transferred by the conveyance; and
- (5) if such conveyance is made as security for indebtedness, the amount and date of maturity of such indebtedness.

### *Regulations.*

(e) The Authority is authorized to provide by regulation for the endorsement upon certificates of registration, or aircraft certificates, of information with respect to the ownership of the aircraft for which each certificate is issued, for the recording of discharges and satisfactions of recorded instruments and other transactions affecting title to, or interest in, aircraft, and for such other records, proceedings, and details as may be necessary to facilitate the determination of the rights of parties dealing with civil aircraft of the United States.



*Previously Unrecorded Ownership.*

(f) The person applying for the issuance or renewal of an air-worthiness certificate for an aircraft with respect to which there has been no recordation of ownership as provided in this section shall present with his application such information with respect to the ownership of the aircraft as the Authority shall deem necessary to show the persons who are holders of property interests in such aircraft and the nature and extent of such interests.<sup>3</sup>

\* \* \* \* \*

(49 U. S. C. 1946 ed., Sec. 523.)

Regulations of Administrator of Civil Aeronautics on  
Civil Aviation, 14 Code of Federal Regulations, 1947  
Supp.:

PART 503<sup>4</sup>—RECORDATION OF AIRCRAFT OWNERSHIP.

§503.1. *Basis and purpose.* The purpose of this part is to prescribe regulations for recordation of conveyances affecting the title to, or interest in, any aircraft registered under the provisions of section 501 of the Civil Aeronautics Act of 1938, as amended (52 Stat., as amended; 49 U. S. C. 521), and of Part 501 or Part 502 of this chapter. The basis for this part is found in sections 308 and 503 of the Civil Aeronautics Act of 1938, as amended.

§503.2. *Definitions.* As used in this part, "Conveyance" means a bill of sale, contract of conditional sale, mortgage, assignment of mortgage, or other instrument affecting title to, or interest in, aircraft.

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<sup>3</sup>Section 503 was amended by the Act of June 19, 1948, c. 523, 62 Stat. 494, but the amendment was subsequent to the last material date in this case (namely, June 15, 1948, when the last aircraft was purchased by the appellee) and hence inapplicable here.

<sup>4</sup>Effective May 1, 1947. See 12 Federal Register 2805.

§503.3. *Eligibility of conveyances.* A conveyance shall be eligible for recordation only if:

(a) It is executed upon the form prescribed by the Administrator for such type of conveyance, or upon a form deemed by the Administrator to be its equivalent; and

(b) It is accompanied by a duly executed application for registration and the required registration fee, and complies with the other provisions of either §501.3(a) or (b) of this chapter, whichever is applicable: *Provided*, That this paragraph shall not apply to conveyances affecting an interest in, but not title to, the aircraft; and

(c) It affects an aircraft currently registered under the terms of the Civil Aeronautics Act of 1938, as amended; and

(d) It states the interest in the aircraft of the person by whom such conveyance is made or given, or in the case of a contract or conditional sale, the interest of the vendor; and, except in cases where the conveyor is the record title holder of such aircraft in the records of the Administrator, it is accompanied by a bill or bills of sale or similar instrument or instruments establishing title to such aircraft in the conveyor; and

(e) It states the interest transferred by the conveyance; and

(f) It is accompanied by the required recordation fee (see §651.53 of this chapter): *Provided*, That this paragraph shall not apply to any conveyance accomplished by a bill of sale or similar instrument transferring title to an aircraft to the purchaser; and

(g) It is acknowledged before a Notary Public or other officer authorized by law of the United States, or a State, Territory, or possession thereof, or the District of Columbia, to take acknowledgment of deeds.

PART 651<sup>5</sup>—PROCEDURE OF THE CIVIL AERONAUTICS  
ADMINISTRATION.

\* \* \* \* \*

*Subpart E—Recordation of Aircraft Conveyances.*

§651.51. *General.* All conveyances which affect the title to, or interest in, any aircraft registered under the provisions of the Civil Aeronautics Act are eligible for recordation with the Civil Aeronautics Administration. Upon receipt of any such conveyance, it is entered upon the Administration's record of conveyances. A receipt showing the recording of any document evidencing indebtedness will be furnished to the holder of such document.

§651.52. *Forms of conveyance.* The following forms have been prepared by the Administrator for use in recording of conveyances and are available upon request to the Certification and Recordation Section, Civil Aeronautics Administration, Washington 25, D. C.

(a) *Form ACA 500: Part C. Bill of Sale.* (For further information concerning Form ACA 500, see §651.31(c).)

(b) *Form ACA 506: Release.* (This form appears on the back of a letter acknowledging receipt of a chattel mortgage and should be in the possession of the mortgagee or his assignee to be used when the mortgage is cleared.)

(c) *Form ACA 818: Release Contract of Conditional Sale.* (This form appears on the back of a letter acknowledging receipt of a contract of conditional sale and should be in the possession of the seller or his assignee to be used when all conditions of the contract have been met.)

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<sup>5</sup>Effective May 1, 1947. See 12 Federal Register 2806.

(d) *Form ACA 905: Aircraft Chattel Mortgage.*

(e) *Form ACA 906: Aircraft Conditional Sale Contract.*

(f) *Form ACA 909: Supplemental Affidavit to Application for Registration for All Types of Aircraft.* (To be filled in and submitted with Application for Registration (Form ACA 500, Part B), when the aircraft has been repossessed pursuant to the provisions of a chattel mortgage or contract of conditional sale and the person repossessing desires registration of the aircraft in his name.)

§651.53. *Application.* A conveyance may be recorded by submitting the original document, or a properly executed duplicate thereof, to the Director, Aircraft and Components Service, Civil Aeronautics Administration, Washington 25, D. C. There is no fee (other than the \$4.00 registration fee) for recording a bill of sale. A fee of \$4.00 is charged for the recording of a lien covering one aircraft. If more than one aircraft is covered by such lien the fee shall be \$4.00 for each aircraft. Fees shall be submitted in the form of a check or money order made payable to the Treasurer of the United States. No fee is required for the recording of a satisfaction of a lien.

§651.54. *Requirements.* For further information with respect to the requirements and instructions for the recordation of aircraft conveyances, see Part 503 of this chapter, or mail request to the Director, Aircraft and Components Service, Attention: Certification and Recordation Section, Civil Aeronautics Administration, Washington 25, D. C.





No. 12347

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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UNITED STATES OF AMERICA,

*Appellant,*

*vs.*

ALL AMERICAN AIRWAYS, INC.,

*Appellee.*

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Appeal From the United States District Court for the  
Southern District of California  
Central Division

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BRIEF OF APPELLEE, ALL AMERICAN  
AIRWAYS, INC.

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GUTHRIE, DARLING & SHATTUCK,  
737 Pacific Mutual Building,  
Los Angeles 14, California,  
*Attorneys for Appellee.*

HALE, STIMSON & RUSSELL,  
122 East 42nd Street,  
New York 17, New York,  
*Of Counsel.*

**FILED**

JAN 10 1950

**PAUL P. O'BRIEN,**  
CLERK



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No. 12347

IN THE

**United States Court of Appeals**  
FOR THE NINTH CIRCUIT

---

UNITED STATES OF AMERICA,

*Appellant,*

*vs.*

ALL AMERICAN AIRWAYS, INC.,

*Appellee.*

---

**BRIEF OF APPELLEE, ALL AMERICAN  
AIRWAYS, INC.**

---

**I.**

**Statement of the Case.**

Appellant's jurisdictional outline and statement of the case are adequate and will not be restated here.

**II.**

**The Issue.**

The sole issue of this appeal revolves around the proper construction of two sections of the United States Code. While there are other sections of ancillary interest, 26 U. S. C. 3672 and 49 U. S. C. 523 are the focal points of the dispute.

26 U. S. C. 3672 is a general statute providing that a federal tax lien "shall not be valid as against any mortgagee, pledgee, purchaser or judgment creditor until notice thereof has been filed by the Collector," in accordance with its provisions, which involves generally recordation at the county where the property may be situated.

49 U. S. C. 523 provides that no "bill of sale, contract of conditional sale, mortgage, assignment of mortgage, or

other instrument affecting title to, or interest in," aircraft shall be valid against innocent third parties unless recorded with the Administrator of Civil Aeronautics.

Appellee, relying upon the provisions of 49 U. S. C. 523 and finding no record of any tax lien or other claim in the office of the Administrator of Civil Aeronautics, purchased three Douglas DC-3 airplanes from Northern Airlines, Inc., the registered owner. Subsequent to the purchase appellee was advised by the Commissioner of Internal Revenue that prior to the purchase a notice of tax lien against Northern Airlines, Inc. totaling \$30,547.80, including interest and penalties, had been filed under 26 U. S. C. 3672 in King County, Washington. Appellant admits that notice of the tax lien was not filed with the Administrator of Civil Aeronautics pursuant to 49 U. S. C. 523 and that appellee had no actual notice of the claimed tax lien at the time of the purchase.

The question is whether the District Court was correct in holding that 49 U. S. C. 523 establishes, for the protection of innocent third parties, a system for recording in a single agency all claims against aircraft, including federal tax liens, or whether recordation under 26 U. S. C. 3672 alone of a federal tax lien against aircraft takes priority over innocent third parties. In other words, in using the term "or other instruments affecting title to, or interest in" did the Congress mean what the words plainly mean or did the Congress mean "or other instruments, *except notices of federal tax liens.*"

Stated still another way, and perhaps more bluntly, the question is whether 49 U. S. C. 523 should be interpreted in a manner that will make it a sensible, useful and needed law or in a manner that will make it senseless and worse than useless.

### III.

#### Summary of Argument.

The language of both 26 U. S. C. 3672 and 49 U. S. C. 523 supports the judgment below. 49 U. S. C. 523 is an all-inclusive statute embracing *all* instruments affecting title to one specific, special type of personal property—aircraft. To construe the statute in any other way would be to reduce it to a meaningless obstruction in the sale and financing of aircraft. 26 U. S. C. 3672, on the other hand, relates only to the validity of federal tax liens with respect to property in general—real and personal. The construction placed on 49 U. S. C. 523 by the District Court gives it life and purpose and does not destroy or impair 26 U. S. C. 3672. The construction urged by appellant would destroy 49 U. S. C. 523 without benefiting 26 U. S. C. 3672.

The history of the two statutes further establishes the validity of the ruling of the Lower Court. 26 U. S. C. 3672 is the outgrowth of the efforts of the Congress to provide broad and general protection to innocent parties against unknown federal tax liens. 49 U. S. C. 523 reflects a recognition by the Congress of the special and peculiar nature of aircraft which requires that innocent parties be given supplemental and special protection against tax liens as well as all other types of liens and claims. The two sections are not antagonistic or in any wise inconsistent.

Application of the fundamental rules of construction leaves no doubt as to the correctness of the District Court's decision.

Finally, an analysis of appellant's argument fails to disclose any valid reason for disturbing the judgment of the District Court.



IV.  
ARGUMENT.

A. 49 U. S. C. 523 Is an All-Inclusive Statute Dealing With Recordation of All Claims to Any Interest in Aircraft, and the District Court in Refusing to Subvert the Purpose of Congress by so Holding Did Not Err.

A brief examination of the language of 49 U. S. C. 523 exposes its all-inclusive nature. At the outset it provides:

“The Administrator shall establish and maintain a system for the recording of *each* and *all* of the following: (1) *Any* conveyance which affects the title to, or *any* interest in, *any* civil aircraft of the United States.”<sup>1</sup>

The term “conveyance” is defined in 49 U. S. C. 401, Subsection 18:

“‘Conveyance’ means a bill of sale, contract of conditional sale, mortgage, assignment of mortgage, or *other instrument affecting title to, or interest in, property.*”

These two sections when read together provide that “The Administrator shall establish and maintain a system for the recording of *each* and *all* of the following: (1) *Any*

---

<sup>1</sup>Emphasis in quoted material added throughout unless otherwise noted.

The quotation is taken from 49 U. S. C. 523 as amended on June 19, 1948, which was subsequent to the last material date in this proceeding, as noted by appellant on page 10 of the appendix to its brief. However, the principal purpose of the amendment was to include aircraft parts. At the same time the language of the section was refined but without affecting the basic objectives of the original wording.



bill of sale, contract of conditional sale, mortgage, assignment of mortgage, *or other instrument affecting title to*, or interest in, *any* civil aircraft of the United States.” The all-embracing and specific nature of this language is apparent. The repetition of such absolute words as “each,” “all” and “any” is significant. Congress enumerated as many of those types of claims which affect title as it thought necessary and then included the term “other instrument” in order to insure against any omission. Exceptions hardly could be inferred from such language.

*Baltimore National Bank v. State Tax Commission*, 297 U. S. 209 (1936), 80 L. Ed. 586, involved the taxation by a state of stock of a national bank owned by Reconstruction Finance Corporation. A federal act (U. S. C., Title 12, Section 548), provided that *all* shares of a national banking association whose principal place of business was within the limits of a state were subject to taxation at the pleasure of the legislature of the state. The bank claimed immunity from the tax on its shares on the ground that all of the shares were owned by Reconstruction Finance Corporation. Justice Cardoza had this to say:

“This court has held that Congress in saying ‘all’ meant exactly what it said, and that shares in a national bank belonging to another national bank were taxable to the same extent as if they belonged to anyone else. (p. 212.)

\* \* \* \* \*

“True, as we have assumed, the Reconstruction Finance Corporation is a governmental agency, but

so also is a national bank. *M'Culloch v. Maryland*, 4 Wheat. 316, 4 L. ed. 579, *supra*. The question thus reduces itself to this, whether there is sufficient reason to believe that immunity from taxes of this kind has been given to the one agency, though by long accepted decisions it has been denied to the other.

*"In such a situation the burden is heavily on the suitor who would subject the word 'all' with its uncompromising generality to an unexpressed exception.* The petitioner reminds us that the ends to be served by the Reconstruction Finance Corporation are even more predominantly public than those of a national bank, since the bank, while promoting the fiscal needs of the government, is acting at the same time for the profit of its stockholders. The suggestion has its force, but force inadequate, we think, to carry to the goal. Its inadequacy is the more apparent when the capacity of the corporation to become a subscriber to the stock is followed to the sources. (pp. 212-3.)

\* \* \* \* \*

"All shares in national banks—no matter by whom owned—shall be subject to taxation. Rev. Stat. Sec. 5219, U. S. C. A. title 12, Sec. 548. Across the petitioner's path there still lies the stumbling block of the uncompromising 'all'." (p. 215.)

That the language of Section 523 was intended to be all-inclusive is further substantiated by placing Section 523 in its setting as a part of Subchapter V of Chapter 9 of Title 49 of the United States Code, which deals with "NATIONALITY AND OWNERSHIP OF AIRCRAFT." In Sec-

tion 521, which is also a part of that subchapter dealing with the recordation of nationality of aircraft, Congress, when desiring to exempt "aircraft of the national defense forces of the United States" felt compelled to do so *expressly*. With this evidence of Congress' concept of the all-inclusive nature of the provisions, there can be no doubt that had an exception in the case of federal tax liens been intended it would have been expressed.

26 U. S. C. 3672, in contrast, is a general recording statute. It is not an exclusive statute nor does it purport to lend validity to a federal tax lien, but rather provides that "such lien shall not be valid as against any mortgagee, pledgee, purchaser or judgment creditor" unless its provisions are complied with. That 26 U. S. C. 3672 is not the exclusive provision limiting the effectiveness of federal tax liens is manifest from a brief review of the cases. Federal estate tax liens have been excluded from the provisions of 26 U. S. C. 3672 and the provisions of 26 U. S. C. 827 held controlling. (*Detroit Bank v. the United States*, 317 U. S. 329, 63 Sup. Ct. 297, 87 L. Ed. 304 (1943).) By the terms of that section any "property sold . . . to a bona fide purchaser for an adequate and full consideration in money or money's worth shall be divested of the lien." In *The River Queen*, *The Dispatch II*, *The Eva Leigh*, 8 F. 2d 426 (1925), a federal tax lien, properly recorded under 26 U. S. C. 3672 and otherwise valid, was held ineffective against a maritime lien which was held to be superior in right. In *In re Holmes Mfg. Co.*, 19 F. 2d 239 (1927), a properly re-

corded income tax lien was held secondary to the obligations incurred by a receiver under a court order, the court saying:

“It does not seem to me that it was the intention of Congress in enacting Section 3186 [now 26 U. S. C. 3670 and 3672] to secure a lien to the government of property in the hands of the receiver which is insufficient in amount to pay the expenses of the receiver incurred under the order of the court upon the filing of the claim for taxes.”<sup>2</sup>

An examination of 26 U. S. C. 3672 makes obvious the conclusion that its entire purpose is to establish a means of helping to protect innocent purchasers from the dangers of secret tax liens upon property in general. Consequently, any statute furthering or bolstering this purpose, such as 49 U. S. C. 523, could not be out of harmony with or contrary to the provisions of 26 U. S. C. 3672. It should be remembered that the reason for recording laws is to make it possible for persons interested to discover with reasonable ease the existence of liens. (*Alcus v. City of New Orleans, La.*, 187 So. 557.)

On the basis of the language of the statutes alone, this appeal should be resolved in appellee's favor.

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<sup>2</sup>See also *Schmitz v. Stockton*, 151 Kan. 891; 101 P. 2d 962; *Regan v. Metropolitan Haulage Company*, 127 N. J. Equity 487, 14 Atl. 2d 257.



**B. The History of 26 U. S. C. 3672 and 49 U. S. C. 523 Supports the Decision of the Lower Court.**

The provisions of the Internal Revenue Code upon which appellant relies are the result of a gradual evolution in tax legislation. Before the amendment of March 4, 1913, which became 26 U. S. C. 3672, a federal tax lien was valid as against subsequent purchasers and encumbrancers without notice and there was no provision for the filing or recording of a notice of lien. It was in reply to justified and vigorous criticism that Congress amended the law to provide for protection of bona fide mortgagees or purchasers against a federal tax lien which was not filed at the time of the mortgage or purchase.<sup>3</sup>

While these amendments in the Revenue Statutes were being enacted, more effective and entirely new statutory provisions were being made necessary by developments in the field of aviation. Despite the attempt at federal regulation through the Air Commerce Act of 1926, Congress was faced in 1938 with a scene of confusion resulting from the complete lack of organization in the handling of aircraft problems.

“At that time three departments of our government were each striving to do their part in promoting aviation. These departments, each doing its best in its own way, were not co-operating, not co-ordinated in their activity. The result was, as might be expected, confusion and lack of initial responsibility. The industry was impaired, investment discouraged and confusion and lack of co-operation was present as re-

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<sup>3</sup>Federal Tax Liens, 105 A. L. R. 1244 at 1250; Federal Taxes and Preferred Ship Mortgages, 38 Harvard Law Review 1060; Merton's Law of Federal Income Taxation, Vol. 9, §54.42 at 608.



gards that which in all human activity should exist—synchronized co-operation between employer and employee.”<sup>4</sup>

To consider the solution to this problem the President of the United States, under the Air Mail Act of 1934 (39 U. S. C. 461-465), provided for the creation of a presidential commission known as the Federal Aviation Commission. This Commission reported to Congress on January 26, 1935, its “Study and survey, and . . . its recommendations of a broad policy covering all phases of aviation and the relation of the United States thereto.” One hundred and two separate recommendations were made by the Commission. Recommendation 101, together with the accompanying discussion, reveals that the Commission considered the problem of proper recordation of matters affecting title to aircraft as involved in the over-all confusion to be resolved. Recommendation 101 reads:

“The application of general legal principles to matters specifically aeronautical should be modified as experience has shown to be wise, *and in particular there should be provisions for federal recording of title to aircraft and of mortgages and OTHER LIENS.*

“It has been inevitable that the rapid changes in aeronautics, together with the administrative experience gained in the control of a new and growing industry, would require changes from time to time in the organic legislation pertaining to the subject. The Air Commerce Act of 1926 has already manifested the wisdom of its sponsors and their foresight

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<sup>4</sup>Senator Pat McCarran, co-author of the Civil Aeronautics Act of 1938, in the foreword to the Civil Aeronautics Act Annotated, by Charles S. Rhyne (1939).

through its ability to meet the needs of aviation development over a period of eight years. Re-examining the subject after that length of time, however, it now appears to us and to legal authorities whom we have consulted that certain changes would be desirable. Largely upon the suggestions of representatives of the Bureau of Air Commerce, whose daily experience with the provisions of the Act warrant careful consideration of their proposals, it is recommended that the Act be so amended as (1) to restate the provision for the registration of aircraft for purposes of nationality; (2) to provide where possible for the recording of title to aircraft; (3) to provide where possible for the recording of *mortgages and/or other liens* upon aircraft; (4) to authorize further safety and public-health regulations; (5) to restate the licensing procedure and to provide additional authorization therefor; (6) to authorize the classification and rating of all air navigation facilities; and (7) to clarify the definitions of terms used in the Act. *The second and third of these seven proposals seem to us particularly important, as designed to give aircraft a legal stability as property that they have never heretofore possessed."*

As a result of these recommendations numerous bills were entered in Congress. The present Civil Aeronautics Act was the culmination of the work of Mr. Lea in the House of Representatives and Mr. McCarran in the Senate and was drafted substantially in its present form by an inter-departmental committee appointed by the President in the late summer of 1937, comprised of representatives of the departments of State, Commerce, Post Office, *Treasury*, War and Navy. Particular note should be made of the fact that the Treasury Department, of which, of course,

the Bureau of Internal Revenue is an integral part, actively participated and was present at the inception of the legislation which became the Civil Aeronautics Act. Mr. Clinton M. Hester represented the inter-departmental committee at the hearing before both the Committee on Interstate and Foreign Commerce of the House of Representatives and the Commerce Committee of the Senate. In this connection the following excerpts from the hearing before the Committee on Interstate and Foreign Commerce of the House of Representatives, 75th Congress, 3rd Session, on H. R. 9738, taken from the Committee Proceedings on Friday, April 1, 1938, at page 405 of the report of those hearings, are pertinent:

“Chairman: Mr. Hester, on page 59 there is a provision for recording of transfer of aircraft owner’s records. I wish you would comment briefly on that.

‘The authority shall establish and maintain a system of recording all conveyances affecting the title to and interest in any civil aircraft of the United States.’

Mr. Hester: If I may, I will ask Mr. Fagg to comment on that.

Mr. Fagg: . . . At the present time and for the past ten years there has been an attempt to record the title for owners of aircraft in the United States that are owned by citizens of the United States; but such recording has been wholly for purposes of determining the nationality of the aircraft. In other words, that has been a step which was provided in the law for the licensee of the aircraft under the provision of the 1926 law.

That has long been felt to be unsatisfactory and particularly when the Reconstruction Finance Corpo-

ration began to make loans, they felt that there should be some protection and many private owners have long felt that *there should be some agency of the Government wherein any interest in aircraft could be recorded for their own protection, because the buyer of a private airplant is up against a problem far worse than that of a purchaser, let us say, of an automobile. Because aircraft can be moved so rapidly from State to State, State recording laws in their individual differences have worked a hardship on the buyer rather than really aided him.* One step in that direction would be, of course, to have a uniform State law; but the possibilities of getting that at an early date seemed to be somewhat remote, and with that thought in mind, *it has been suggested that the Federal Government serve that want by setting up a title recording agency within this civil aeronautic authority.*

Mr. Boran: Will you permit a question there, Mr. Fagg?

Mr. Fagg: Yes.

Mr. Boran: Have there been, to your knowledge, numerous instances of faulty title to aircraft because of this condition?

Mr. Fagg: Yes sir; there have been many complications, Mr. Boran, that have arisen as to whether or not we should license aircraft, because we firmly believe we do not possess all of the facts. There have been many cases that have been embarrassing to us in the mere recordation of titles for the purpose of nationality."

It was under the glare of this illuminating background that Congress included the central recording provision in the Civil Aeronautics Act of 1938, which Act had as its



purpose "to co-ordinate in a single independent agency all of the existing functions of the federal government with respect to civil aircraft, and in addition, to authorize the agency to perform certain new and regulatory functions which are designed to stabilize the air transportation industry in the United States."<sup>5</sup>

The reasons for the creation of a single agency to handle all phases of the aircraft problem were well explained in the report from the Committee on Interstate and Foreign Commerce of the House of Representatives:

"Careful consideration was given by your committee to the question as to the desirability of creating an independent agency to regulate civil aeronautics. Due to the unique character of the regulatory problem presented by civil aeronautics, it was concluded by your committee that for the present the most efficient and advantageous regulation, both from the standpoint of the public interest and from that of the industry to be regulated, could be secured by the co-ordination of *all governmental functions relating to civil aeronautics in a newly created independent agency.*"<sup>6</sup>

The purpose of including 49 U. S. C. 523 in the general plan of unification was clarified by the Honorable Fred Fagg, presently the President of the University of Southern California, in his testimony before the Committee on Interstate and Foreign Commerce of the House of Representatives as "primarily aimed to make a *central*

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<sup>5</sup>Report from the Committee on Interstate and Foreign Commerce, No. 2254, Series 10234, to accompany H. R. 9738.

<sup>6</sup>Report from the Committee on Interstate and Foreign Commerce, No. 2254, Series 10234, to accompany H. R. 9738, at page 4.



*clearinghouse for recordation* of titles so that a person, wherever he may be, will know where he can find ready access to the *claims against or liens or other legal interests* in an aircraft." In Civil Aeronautics Act Annotated, by Charles S. Rhyne, when referring to the statement made by Mr. Fagg before the Committee of the House of Representatives, the author noted:

"This statement directly relating to recordation states the exact problem that Congress intended to solve by requiring recordation. Some other past experiences of private persons demonstrate the need for centralized and adequate recording records, which all purchasers can check before purchasing an airplane" (p. 151).

This brief historical sketch of the Civil Aeronautics Act of 1938 exposes the intent of Congress in enacting it. The Act was designed to lend order where there had been confusion, not the least of which was in the field of recordation of titles and claims to aircraft. It was designed to concentrate in a single agency all matters affecting aircraft. At the time of its passage Howard S. Leroy, writing in 19 *Air Law Review* 315, observed:

"The administrative regime is comprehensive, fully integrated and calculated to govern the art for the foreseeable future."

Included in this comprehensive and integrated regime was the provision for the centralized recordation of titles and claims to aircraft.

In response to this purpose and intent the Court in *In the Matter of Veterans' Air Express, Inc.*, 76 Fed. Supp. 684 (D. C. N. J., 1948), made this observation concerning 49 U. S. C. 523:

"It is clear that the Congress has prescribed the *only way* in which aircraft may be transferred and in which *liens* upon aircraft may be duly recorded. In this manner all persons dealing with aircraft are upon full legal notice concerning possible liens and are charged with the duty of inquiry at the Central Recording Office of the Civil Aeronautics Administration with respect to any aircraft in which they might be concerned" (p. 688).

Likewise in *United States v. United Aircraft Corp.*, 80 Fed. Supp. 52 (D. C. Conn., 1948), the court said:

"The Congress has pre-empted the field of conveying of interests in aircraft and portions thereof to facilitate the control and promotion of air commerce. The power to do so may not be denied . . . *The recording system for aircraft covers the entire United States*"<sup>7</sup> (p. 54).

That these opinions were shared by Congress and acted upon in 1948 is evidenced by the language employed in the report of the House Committee on Interstate and Foreign

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<sup>7</sup>In *Wilson v. Barnes, et al.*, 221 S. W. 2d 731 (June 13, 1949), the Supreme Court of Missouri relied upon *United States v. United Aircraft Corporation*, and *In re Veterans Air Express Co., Inc.*, in sustaining a writ of attachment levied on ten airplanes against a third party claim which was not recorded in accordance with 49 U. S. C. 523. The Supreme Court of Georgia in *Blalock v. Brown*, 78 Ga. A. 540, 51 S. E. 2d 610 (February 3, 1949), also cited with approval *United States v. United Aircraft Corporation* and *In re Veterans Air Express Co., Inc.*, and held the defendant's title in an airplane recorded at the office of the Administrator of Civil Aeronautics under 49 U. S. C. 523 superior to plaintiff's claim under a prior unrecorded conveyance.

Commerce on the amendments then enacted to 49 U. S. C. 523 concerning spare parts:

“The Committee on Interstate and Foreign Commerce, to whom was referred the bill (S. 2454), to amend the Civil Aeronautics Act of 1938, as amended, to make further provision for the recording of title to, *interests in*, and *encumbrances upon* certain aircraft, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.”

\* \* \* \* \*

“This bill would provide a system for the recordation of *liens* on large aircraft engines and on spare parts used by air carriers. *The Civil Aeronautics Act now provides that the Administrator maintain a system for the recordation of all conveyances affecting title to, or interest in, aircraft of the United States.* That system has been in operation successfully for 10 years, but does not permit the recordation of liens on aircraft engines or spare parts maintained for installation in aircraft. This bill would broaden the present provisions to permit that type of recordation.”<sup>8</sup>

The amendment of 1948 was intended to implement an already existing system for recordation of liens on aircraft by the addition of liens upon parts of the airplanes. The whole purpose of this amendment, as well as the basic provision of the statute, would be defeated if any omission or exception in the record of title in the office of the Civil Aeronautics Board were permitted by judicial interpretation.

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<sup>8</sup>United States Code Congressional Service (1948), Vol. 2, page 1896.

Unless the very purpose of the centralized recording system for aircraft, as set up by 49 U. S. C. 523, is to be completely stultified, the United States Government must record its claim of tax lien on an aircraft in compliance with that centralized procedure to the same extent as is required of the most humble citizen if he wishes to protect his interest in an aircraft against the claims of an innocent third party. If a purchaser of aircraft could rely on the central recording agency only for all adverse claims, interests or liens, except a claim of the United States Government for a tax lien, the benefits of the central recording system would be little more than zero. To be certain of the validity of his title to the aircraft being purchased he would still have to search the records of every county of every state of the United States to be sure that the government had no claim of a tax lien. If required to make this collateral search for a government tax lien he might just as well be searching at the same time for all other liens and claims. Thus, if a single exception be admitted to the Act through judicial construction, the entire Act should be repudiated, as the state of confusion stemming from a single exception would be quite as complete as it was before the Act was placed in the books.

It is not sensible to conclude that Congress could have intended to set up a centralized procedure for recordation and at the same time defeat its purpose of providing certainty in transactions dealing with aircraft by eliminating tax liens from the requirements of central recordation. Such a conclusion becomes impossible when it is realized that the impression given Congress throughout the testimony of Mr. Fagg was that the Act provided "a central clearing-house . . . where" a purchaser could find "ready access to the claims against, or *liens*, or other legal interests in aircraft" and that this testimony of Mr.



Fagg was given at the request of the representative of the Treasury Department, Mr. Clinton M. Hester. Mr. Hester by his own testimony<sup>9</sup> was the chairman of the subcommittee of three which was in charge of the drafting of the bill. He was also chief counsel of the Treasury Department heading a staff which devoted itself largely to the drafting of legislation in which the Treasury Department was interested.

There is a certain aura of bad faith about the position of the representatives of the Treasury Department now eleven years later seeking to contradict the explicit impression given Congress.

“Words generally have different shades of meaning, and are to be construed, if reasonably possible, to effectuate the intent of the lawmakers; and this meaning in particular instances is to be arrived at not only by a consideration of the words themselves, but by considering, as well, the context, the purposes of the law, and *the circumstances under which the words were employed.*”

*People of Puerto Rico v. Shell Oil Co.*, 302 U. S. 253, 58 Sup. Ct. 167, 82 L. Ed. 235.

The words of the statute itself, its context, its purposes and the circumstances under which it was enacted all conclusively establish the intention of Congress to provide a means for the recordation of *all* claims against aircraft with one agency where prospective purchasers, such as appellee, might satisfy themselves of the safety of their contemplated investment or purchase.

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<sup>9</sup>Report of the hearings before the Committee on Interstate and Foreign Commerce of the House of Representatives, at page 48 of the report of the hearings.



C. Application of Fundamental Rules of Construction Leaves No Doubt as to the Correctness of the Decision of the Lower Court.

"There can be no question that the court must be guided by the elementary rule of construction, that, wherever possible, the language will be interpreted so as to give effect to the object sought to be accomplished."

*Madison Park Corp. v. Bowles*, 140 F. 2d Em. App. 360.

The object sought to be accomplished by Congress in the enactment of 49 U. S. C. 523 cannot be denied. As has been demonstrated, Congress intended to establish "centralized and adequate recording records which all purchasers can check before purchasing an airplane."<sup>10</sup> Applying the elementary rule of construction of effectuating this intent, the District Court was correct in construing 49 U. S. C. 523 to apply to *all* claims of interest in aircraft, including tax liens.

This first rule of construction is followed closely, if not accompanied, by the rule cited in *Bird v. The United States*, 187 U. S. 118, at 124, 23 Sup. Ct. 42, 47 L. Ed. 1245:

"There is a presumption against a construction which would render a statute ineffective or insufficient, or which would cause grave public injury or even inconvenience."

The case here at issue offers an excellent example of the injuries that would accrue if the construction now

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<sup>10</sup>Charles S. Rhyne in *Civil Aeronautics Act Annotated* (1939) at page 151.

urged by appellant were adopted. Appellee, All-American Airways, Inc., with its offices and operations in the east, is a commercial airline holding a certificate of public convenience and necessity issued by the Civil Aeronautics Board under the Act of which the statute with which this appeal is concerned forms a part. It is perfectly reasonable to assume that appellee has an attorney familiar with aviation law in general, and the Civil Aeronautics Act in particular, including 49 U. S. C. 523, and that appellee was advised by its counsel that a search of the instruments on record at the centralized agency pursuant to 49 U. S. C. 523 would be sufficient to assure clear title to the three airplanes involved in this appeal. Thus a federally certificated airline operating under the Civil Aeronautics Act for more than ten years and guided by experienced counsel, construed 49 U. S. C. 523 as the Lower Court construed it and relied on that construction. The \$30,000.00 which appellee would lose by an erroneous decision in this proceeding is grave enough. But the damage to the entire commercial airline industry, as well as the public at large, transcends the injury which appellant would sustain, grave as that might be.

Again in *Haggar Co. v. Helvering*, 308 U. S. 389, at 394, 84 L. Ed. 340, at 344, Justice Stone stated the rule:

“All statutes must be construed in the light of their purpose. A literal reading of them which would lead to absurd results is to be avoided when they can be given a reasonable application consistent with their words and with the legislative purpose.”

Finally, the rule has been restated recently in *Vermilya-Brown Co. v. Connell*, 93 L. Ed. 99, at 105, Adv. Opin. (December 6, 1948), where the Supreme Court was considering the meaning of the word "possession" in the Fair Labor Standards Act as extending that Act to the lend-lease base at Bermuda:

"What was said of 'territories' in the *Shell Co. Case*, 302 U. S. 253, at 258, 82 L. ed. 235, 240, 58 S. Ct. 167, is applicable:

'Words generally have different shades of meaning, and are to be construed if reasonably possible to effectuate the intent of the lawmakers; and this meaning in particular instances is to be arrived at not only by a consideration of the words themselves, but by considering, as well, the context, *the purposes of the law*, and the circumstances under which the words were employed.'

The word 'possessions' has been employed in a number of statutes both before and since the Fair Labor Standards Act to describe the areas to which various congressional statutes apply. We do not find that these examples sufficiently outline the meaning of the word to furnish a definition that would include or exclude this base. While the general purpose of the Congress in the enactment of the Fair Labor Standards Act is clear, no such definite indication of the purpose to include or exclude leased areas, such as the Bermuda base, in the word 'possession' appears. We cannot even say, 'We see what you are driving at, but you have not said it, and therefore we shall go on as before.' *Under such circumstances, our duty as a court is to construe the word 'possession' as our judgment instructs us the lawmakers, within constitutional limits, would have done had they acted at the time of the legislation with the present situation in mind.*"

From these pronouncements of the Supreme Court, it is clear that even if the language of 49 U. S. C. 523 were ambiguous in its application to *all* claims against aircraft, which is not the case, neither this court nor the District Court would be bound by any literal interpretation in effectuating the manifest purpose of Congress. This court is free to examine the Congressional mind for the purpose of determining the applicability of 49 U. S. C. 523 to specific types of claims such as federal tax liens.

Since 26 U. S. C. 3672 is argued by appellant to be in conflict with 49 U. S. C. 523, it is appropriate to mention another rule of construction which may be applied to it:

“It is to be remembered that we are dealing with a tax measure, and whatever doubts exist must be resolved against it.”

*Schwab v. Doyle*, 258 U. S. 529, 42 Sup. Ct. 391, 66 L. Ed. 747.

This rule was restated in *White v. Aronson*, 302 U. S. 16, at 20, 82 L. Ed. 20, at 23: “Where there is a reasonable doubt as to the meaning of a taxing act, it should be construed most favorably to the taxpayer.” And again in *Hassett v. Welch*, 303 U. S. 303, 82 L. Ed. 858, in which the court found against the government:

“In view of other settled rules of statutory construction, which teach \* \* \* that, if doubt exists as to the construction of a taxing statute, the doubt should be resolved in favor of the taxpayer.”

It follows that in carrying out the purpose of 49 U. S. C. 523 the court is also aided by an application of



strict rules of construing tax statutes as a repellent to the claimed conflict of 26 U. S. C. 3672.

The statutes here involved also call for application of the general principle that when one statute deals with a subject in general terms, and another deals with a part of the same subject more definitely, and the two are not necessarily repugnant, the special statute will prevail over the general. This is particularly true when the special statute is later in point of time. Where the general statute, if standing alone, includes the same matter as the special statute and thus to that extent conflicts with it, the special act usually will be considered an exception to the general enactment, even though passed before the general enactment. Where the special statute is later it will *always* be regarded as an exception to or qualification of the prior general act.<sup>11</sup>

Here the general statute is 26 U. S. C. 3672 which deals with all types of property, real and personal. The special statute is 49 U. S. C. 523 which deals only with aircraft and aircraft parts—a specific type of personal property.

The special statute pertaining to airplanes was enacted after the general statute and thus it would be proper (if ambiguity or conflict existed) to apply the rule that the special statute, 49 U. S. C. 523, is an exception to, or a qualification of, the general statute, 26 U. S. C. 3672.

In *MacEvoy v. United States*, 64 Sup. Ct. 890, 322 U. S. 102, 88 L. Ed. 1163 (1944), it is said at page 1167 (L. Ed.):

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<sup>11</sup>59 C. J. 1056, 1058.



“However inclusive may be the general language of a statute it will not be held to apply to a matter specifically dealt with in another part of the same enactment. Specific terms prevail over the general in the same or *another statute* which otherwise might be controlling.”

In *United States v. Windle*, 158 F. 2d 196 (8th Cir. Ct., 1946), which dealt with the Internal Revenue Code, it is said at page 199:

“We recognize the rule that generally special terms of a statute prevail over general terms in the same or another statute which otherwise might control  
\* \* \* The purpose of this rule is to give effect to presumed intention of the lawmaking body.”

In *Detroit Bank v. United States*, 317 U. S. 329 (1914), 87 L. Ed. 304, the court held that 26 U. S. C. 3670 and 3672 did not establish the exclusive means by which federal tax liens may be made effective and that estate tax liens become effective pursuant to the provisions of Section 315(a), Revenue Act of 1926. The court noted that the two statutes were intended to operate independently of the other, and that an estate tax lien created by Section 315(a) was not subject to the recordation requirement of Section 3672. In the case at issue, because of the legislative intent in setting up the centralized recording system affecting civil aircraft, the special statute must prevail.

Application of fundamental rules of construction leaves no doubt as to the correctness of the judgment of the District Court applying 49 U. S. C. 523 in a manner which effectuates the Congressional intent.

### D. Appellant's Argument Analyzed.

Appellant's argument appears to consist of four propositions. Simply stated they are:

1. The facts in this case and a reading of 26 U. S. C. 3672 establish the validity of the government's lien.

2. Failure expressly to include federal tax liens within the provisions of 49 U. S. C. 523 excludes them from its provisions.

3. A notice of a federal tax lien is not an instrument affecting title to, or interest in, aircraft, within the meaning of 49 U. S. C. 523.

4. The courts should not be influenced by the incongruous and injurious effects of the interpretation urged by appellant.

#### (1) The Facts in This Case and a Reading of 26 U. S. C. 3672 Establish the Wisdom of the Decision of the District Court.

Appellant's first proposition is that the "facts establish \* \* \* the tax lien of the United States \* \* \* was valid" and "Section 3672 of the Code [Title 26] makes that lien valid."<sup>12</sup> The argument simply begs the question on this appeal. The facts establish only that the United States recorded a tax lien against Northern Airlines, Inc. with the auditor of King County, Washington, and that appellee purchased three DC-3s belonging to Northwest Airlines, Inc. in good faith, relying on the absence of any recorded claim against the title of

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<sup>12</sup>Appellant's Brief, pages 10-12.

Northwest Airlines, Inc. in the office of the Civil Aeronautics Administrator. As has been shown in this brief (pp. 7 and 8), 26 U. S. C. 3672 does not establish the validity of a tax lien but is simply a non-exclusive *limitation* on the validity or effectiveness of the lien. Appellant's contention is like arguing that an unrecorded mortgage is a valid lien between the mortgagor and mortgagee. There is no question about this, but until the mortgagee causes the mortgage to be recorded in accordance with the applicable law he is not protected as against innocent third persons who deal with the property without actual notice of the unrecorded mortgage. It is in this situation that appellant finds itself because it did not see fit to comply with the recording Act that pertains to civil aircraft. Appellee, an innocent purchaser, relied on that omission and should not be penalized because of appellant's default.

**(2) Specific Language Is Not Necessary to Include Federal Tax Liens Within the Provisions of 49 U. S. C. 523.**

Appellant next urges that "a statute which in general terms divests pre-existing rights or privileges will not be applied against the sovereign without express words to that effect"<sup>13</sup> and reasserts its position on page 17 that "The important factor in this case is that the recordation provisions of the Civil Aeronautics Act does not expressly include tax liens created under the Internal Revenue Code."

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<sup>13</sup>Appellant's Brief, pages 12-13.

In support of this claimed rule appellant relies upon *United States v. United Mine Workers of America*, 330 U. S. 258, 67 Sup. Ct. 677, 91 L. Ed. 884. In that case the court at pages 273-4 said:

“There is an old and well-known rule that statutes which in general terms *divest pre-existing* rights or privileges will not be applied to the sovereign without express words to that effect. It has been stated, in cases in which there were *extraneous and affirmative reasons for believing that the sovereign should also be deemed subject to a restrictive statute*, that this rule was a rule of construction only.”

In *Nardone v. the United States*, 302 U. S. 379, 58 Sup. Ct. 275, 82 L. Ed. 314, it was recognized that the rule was subject to limitations and “the cases in which it has been applied fall into two classes. The first is where an act, if not so limited, would deprive the sovereign of a recognized or established prerogative, title or interest.”

There are, therefore, at least two exceptions to the application of this rule of construction, (1) when the government is *not* divested of a pre-existing right or privilege by the statute, and (2) when extraneous and affirmative reasons exist for applying the statute to the government. The statute here involved falls within *both* of the exceptions and, in addition, contains express words bringing the government within its purview.

*The government is not divested of any pre-existing right or privilege by 49 U. S. C. 523.* This statute merely simplifies the procedure for implementing a pre-existing right. Had 49 U. S. C. 523—to resort to a rather grotesque example—proclaimed that no person could obtain any kind of a lien against any civil aircraft, by mortgage or otherwise, appellant might well have had an argument.



But that is not the situation. Under the statute the government can establish its lien by the very simple procedure of recording it with one centralized recording agency. This is an added advantage—not a divestment of a right or privilege.

*Extraneous and affirmative reasons exist for applying 49 U. S. C. 523 to the government.* The purpose of the statute is obvious. An airplane is not like a drill press or house and lot, or even an automobile, all of which have a permanent "residence" and lend themselves to application of local recording rules. This is not true of the airplane, the transitory nature of which places it in a class by itself. To prevent wrongs and to eliminate confusion, the Congress wisely provided for a centralized recording agency with respect to civil aircraft. By searching the records of that single agency, any interested party, including the government and any of its agencies, can check the title to any particular aircraft. If the government were not required to record its lien under 49 U. S. C. 523 the value of a centralized recording agency would be destroyed completely. A single exception to the application of the statute would necessitate a nationwide search, in addition to searching the records of the Civil Aeronautics Board, in order to be certain of the title to any aircraft. These are extraneous and affirmative reasons for believing that the Congress intended that the government also should be held subject to the statute.

*The Civil Aeronautics Act expressly applies to the government.* Even though neither of the two exceptions to the rule of construction urged by appellant were held to apply, the Civil Aeronautics Act very clearly comes within the purview of the rule itself. No case cited by the government, and none that appellee can find, declares that a



statute divesting a pre-existing right or privilege must *name* the government as such.

The Act itself by express words makes it manifest that the sovereign is included. Section 1 of the Act (49 U. S. C. 401) reads in part:

“Section 1. As used in this Act, unless the context otherwise requires—

(27) ‘*Person*’ means any individual, firm, copartnership, corporation, company, association, joint-stock association, or *body politic*; and includes any trustee, receiver, assignee, or other similar representative thereof.”

Section 501 of the Act (49 U. S. C. 521) reads in part:

#### “Registration Required

(a) It shall be unlawful for any *person* to operate or navigate any aircraft eligible for registration if such aircraft is not registered by its *owner* as provided in this section, or (except as provided in section 6 of the Air Commerce Act of 1926, as amended) to operate or navigate within the United States any aircraft not eligible for registration: *Provided, That aircraft of the national defense forces of the United States may be operated and navigated without being so registered if such aircraft are identified, by the agency having jurisdiction over them, in a manner satisfactory to the Administrator of Civil Aeronautics.* The Administrator of Civil Aeronautics may, by regulation, permit the operation and navigation of aircraft without registration by the owner for such reasonable periods after transfer of ownership thereof as the Administrator of Civil Aeronautics may prescribe.

“Eligibility for Registration

(b) An aircraft shall be eligible for registration if, but only if—

(1) It is owned by a citizen of the United States and is not registered under the laws of any foreign country; or

(2) It is an aircraft of the *Federal Government*, or of a State, Territory, or possession of the United States, or the District of Columbia, or of a political subdivision thereof.”

If it were not intended that the Act apply to the government, it would not have been necessary to make an exception with respect to aircraft of the national defense forces of the United States. Moreover, under subdivision (a) of 49 U. S. C. 521 it is unlawful for any *person* to operate or navigate any aircraft *eligible for registration* if it is not registered by its *owner*. Subdivision (b) designates the aircraft that are eligible for registration and includes aircraft of the federal government. Thus the words “person” and “owner” as used in subdivision (a) necessarily must include the federal government. This construction ties with subdivision (27) of Section 1 (49 U. S. C. 401) defining “persons” as including a *body politic*.

The language of the statute here at issue, read with the language quoted in Section 501 (49 U. S. C. 521) and the definition of “person” quoted in Section 1 (49 U. S. C. 401), excludes all validity to any argument that the Civil Aeronautics Act lacks express words to the effect that the United States Government was intended to be subject to its provisions.

At this point a query is pertinent. If the government be not required to record its tax liens against aircraft

under 49 U. S. C. 523, would a chattel mortgage between individuals, recorded under the statute, be valid against the government if the government purchased the aircraft from the mortgagor? The statute states that no conveyance (which includes a chattel mortgage as well as a tax lien) shall be valid against any *person* until the conveyance is recorded in the office of the Secretary of the Board. If the word "person" does not include the government, an individual mortgagee would not be safe in recording under the Act. A construction that the government is not required to record its liens under 49 U. S. C. 523 would be bad enough. A construction that, in addition, a chattel mortgage recorded under the statute would not be valid against the government as a purchaser would lead to vicious consequences. Either construction, necessarily, would carry with it the other if consistency were preserved.

In the same vein it might be asked whether a chattel mortgage on civil aircraft in favor of Reconstruction Finance Corporation and recorded under 49 U. S. C. 523 would be valid against the Treasury Department or any other agency of the government.<sup>14</sup> Other examples could be given of the grotesque consequences which would flow from an acceptance of the crude construction of the statute proclaimed by appellant.

It must be remembered that the rule cited by appellant is "a rule of construction only" (*United States v. United Mine Workers of America*, 330 U. S. 258, 67 Sup. Ct.

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<sup>14</sup>There can be no doubt of the right of this court to take judicial notice of the fact that Reconstruction Finance Corporation holds chattel mortgages on civil aircraft recorded under the statute which involve many millions of dollars loaned to commercial airlines.

677, 91 L. Ed. 884). As such the rule was clarified in *United States v. California*, 297 U. S. 173, 186, 80 L. Ed. 567, 574, by the statement that:

“The presumption is an aid to consistent construction of the statutes of the enacting sovereign when their purpose is in doubt, but it does not require that the aim of a statute, fairly to be inferred, be disregarded because not explicitly stated.”

The principle is further elaborated in *Baltimore National Bank v. State Tax Commissioner*, 297 U. S. 209, 80 L. Ed. 586, “that the sovereign is embraced by general words of a statute intended to prevent injury and wrong.”

Agreement is found in the language of the Supreme Court in *United States v. Rice*, 327 U. S. 742, 90 L. Ed. 982, in holding that Section 2 of the Judiciary Act of March 3, 1887, 28 U. S. C. 71 and 80 applies to deny to the government the right to an appeal or writ of error from the decision of any federal court remanding a case to a state court, although the government is in no way mentioned in the Act. The court stated at pages 752-753:

“Statutory language and objective, thus appearing with reasonable clarity, are not to be overcome by resorting to a mechanical rule of construction whose function is not to create doubts but to resolve them when the real issue or statutory purpose is otherwise obscure.”

In face of the clarity of the law and the background of its enactment appellant's statement on page 17 of its brief that “if it [Congress] had intended that the recordation provisions of the Act apply to liens with respect to civil aircraft, it would have said so specifically” has a hollow ring. When called upon to explain 49 U. S. C. 523,



Mr. Clinton Hester, legislative counsel of the Treasury Department representing the inter-departmental committee which proposed the Civil Aeronautics Act of 1938, introduced Mr. Fred Fagg who asserted that the Act was intended to cover *all* claims. If the Treasury Department wished to controvert that interpretation of the provision the time to have done so was then through its representative, Mr. Hester, instead of eleven years later in this litigation, to the detriment of appellee which innocently relied upon the Treasury Department's own interpretation.

**(3) A Notice of a Federal Tax Lien Is an Instrument Affecting Title to, or Interest in, Aircraft Within the Meaning of 49 U. S. C. 523.**

Appellant's third contention is that "tax liens . . . cannot . . . be regarded as being included in the general phrase 'or other instrument affecting title to, or interest in property' (49 U. S. C. 523)" and seeks to apply the rule of *ejusdem generis* to limit the application of the statute to instruments "used to effect a transfer by an owner of property . . . by affirmative act."<sup>15</sup>

Appellant cites no case limiting the word "instrument" in a recording statute to such a forced definition. To the contrary, in *State v. Phillips*, 157 Ind. 481, 62 N. E. 12, the court considered a statute fixing a fee for the recording of "deeds and mortgages" and providing "for entering on entry book, indexing and recording *all other instru-*

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<sup>15</sup>Appellant's Brief, pages 13-14.



ments.” Plaintiff sought a writ of mandamus to compel the county recorder to enter a notice of a mechanic’s lien. The court granted the writ, saying:

“The word ‘instrument’ in a legal sense is defined to be ‘a writing as the means of giving formal expression to some act; a writing expressive of some act, contract, process, or proceeding, as a deed, contract, writ and so forth.’ Webs. Int. Dic.” (p. 14.)

and:

“The word ‘instrument’ is frequently employed in our registry laws and usually refers to some written document that is entitled to be recorded in a public record.” (p. 14.)

In *Driefus v. Marks, et al.*, 40 Cal. App. 2d 461, 104 P. 2d 1080, the court considered the validity of the recordation of a notice of rescission under Civil Code, Section 1158, which provided in part:

*“Any instrument . . . affecting the title to or possession of real property may be recorded under this chapter.”*

The court held:

“In the language of said code section, said notice of rescission did affect the title to real property. Its effect was to declare to the world that the author of the notice had by the delivery of a deed been defrauded by the party upon whom the notice had been served, or had failed to receive consideration for the deed, which fact was notice of the invalidity of such prior deed.” (p. 466.)

Similarly in this case notice of a federal tax lien was an instrument which appellant might have recorded and

which Congress intended should be recorded at the office of the Administrator of Civil Aeronautics.

In its argument that, under the doctrine of *ejusdem generis*, instruments should be limited to those constituting affirmative acts of the owner of the property, appellant again fails to cite any authority. In *City of Los Angeles v. Superior Court of L. A. County*, 2 Cal. 2d 138, 39 P. 2d 401, the court was presented with a similar argument. Plaintiff, City of Los Angeles, had commenced condemnation proceedings. At the time of the action a street assessment had been filed against the land but was not yet due. The City sought to deduct the amount of the street assessment from the consideration paid to defendant under Code of Civil Procedure, Section 1248, subsection 8, which provided:

“‘When the property sought to be taken is encumbered by a *mortgage or other lien*, and the indebtedness secured thereby is not due at the time of the entry of the judgment, the amount of such indebtedness may be, at the option of the plaintiff, deducted from the judgment, and the lien of the mortgage or other lien shall be continued until such indebtedness is paid.’”

Defendant there urged, as appellant does here, that in using the term “mortgage or other lien” the legislature meant to include liens “created by the property owner” and sought to apply the doctrine of *ejusdem generis*. The court held:

“The rule of construction relied upon is of course not positive or mandatory, but is simply an aid to the ascertainment of the legislative intent. \* \* \* The purpose of the statute is obviously to prevent a situa-

tion wherein the condemnor will pay the full value of the land and thereafter will be forced to pay again to holders of liens on the land when the lien becomes due. *Bearing this purpose in mind, it certainly makes no difference whether the lien was created by the owner, as in the case of a mortgage, or arose in other ways.*" (p. 140.)

As stated by Mr. Fagg in his testimony before the Committee on Interstate and Foreign Commerce of the House of Representatives, 49 U. S. C. 523 is "primarily aimed to make a central clearinghouse for recordation of titles so that a person, wherever he may be, will know where he can find ready access to the *claims against, or liens, or other legal interests in an aircraft.*" To borrow the language of the Supreme Court of the State of California, just cited, "Bearing this purpose in mind, it certainly makes no difference whether the lien was created by the owner, \* \* \* or arose in other ways."

Even a strict application of the rule of *ejusdem generis* would be of no avail to appellant. A bill of sale, a contract of conditional sale, a mortgage and an assignment of mortgage are all "instruments affecting title to, or interest in, property." A notice of tax lien affects the title to property and thus falls within the same general character of the documents specifically named.

If appellant's argument were sound, a judgment quieting title, a notice of *lis pendens*, a mechanic's lien and a decree of distribution in a probate proceeding—to name only four examples—would not be other instruments af-

fecting title to, or interest in, property, as these instruments do not involve “a transfer by an owner of property of some interest or right therein, by affirmative act.”<sup>16</sup> Indeed, if appellant’s theory were applied, the words “or other instrument affecting title to, or interest in, property” would be meaningless. And if a judgment quieting title, a notice of *lis pendens*, a mechanics’ lien, a decree of distribution in probate and a notice of federal tax lien were exempt from 49 U. S. C. 523, the statute itself would be meaningless. It was not the intention of the Congress to employ meaningless words, much less enact a meaningless statute.

The doctrine of *eiusdem generis* is activated to make sense out of legislation, not to make it senseless:

“The rule of *eiusdem generis* is applied as an aid in ascertaining the intention of the legislature, not to subvert it when ascertained.”

*Texas v. the United States*, 292 U. S. 522, 54 Sup. Ct. 819, 78 L. Ed. 1402.

This cardinal principle was elaborated on in *United States Cement Co. v. Cooper*, 172 Ind. 599, 88 N. E. 69, where the court said of the rule:

“It is never to be used in an arbitrary sense.  
\* \* \* Whether or not the doctrine should be applied in any case depends largely upon the character and contents of the Act as a whole, having due regard for that primary rule of construction that the object of the law must be sought from the entire Act, including the title, and from a *consideration of the evil to be remedied*, the state of public sentiment existing

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<sup>16</sup>Appellant’s Brief, page 14.



at the time of the passage of the law, *and the general purpose of the Act* as derived from a consideration of every section. If the general purpose of the legislation clearly appears from a study of all the parts, that purpose cannot be defeated or limited by the doctrine we are considering.”

Appellant's final argument for a nihilistic construction of the word “instrument” is that regulations of the Administrator of Civil Aeronautics require that the interest claimed in the aircraft be stated in the instrument which is to be recorded. Appellant urges that since a federal tax lien applies to after acquired property the interest in a specific aircraft might not be known at the time of recordation. This is a simple, procedural problem, not one of substance, and offers no reason for subverting the intent of Congress. Even under the regulation referred to and criticized by appellant, the government can protect itself with a little vigilance. Vigilance is required of the average citizen in most of his activities and dealings—requiring a little vigilance now and then on the part of the government would not seem to be such a sin.

Moreover, this concern of appellant is not shared by the courts. In *United States v. Maniaci*, 36 Fed. Supp. 293 (D. C. Mich., 1939), a federal tax lien was held subordinate to the rights of an innocent purchaser of real property where the government had not complied with the requirement of Section 3746 of the compiled laws of Michigan to the effect that notice of a lien must contain a description of the land upon which a lien is claimed. The decision was affirmed in 116 F. 2d 935 (Sixth Circuit, 1940) and was followed in *United States v. City of Detroit*, 138 F. 2d 418 (Sixth Circuit, 1943). In *Young-*



*blood v. United States*, 141 F. 2d 912 (Sixth Circuit, 1944), the court, in denying a writ of mandamus to compel the recording of a federal tax lien which did not contain a description of the property against which the lien was claimed, said at page 914:

“Mere inconvenience to federal tax officials in procuring and filing descriptions of land owned by delinquent taxpayers supplies no sound basis for the issuance of peremptory writ of mandamus by federal courts.”

The cases interpreting the language of the type used by Congress, the purpose of the language and the proper use of the rule of *ejusdem generis* support the conclusions of the lower court that federal tax liens are included in the phrase “or other instrument affecting title to, or interest in, property” and that tax liens come within the provisions of 49 U. S. C. 523.

**(4) The District Court Correctly Considered the Purpose of 49 U. S. C. 523.**

Appellant concludes its argument with the contention that, while “the court below might have been influenced by the thought that if a purchaser of aircraft, such as the appellee, could not rely on the Civil Aeronautics recording system as to tax liens, he might be subjected to an endless search of the records of every county in every state,” such a conclusion would be erroneous and that “the courts must not add to the provisions of a statute or supply an omission or question the wisdom of the legislative body in adopting certain provisions and not adopting others.”<sup>17</sup>

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<sup>17</sup>Appellant's Brief, pages 16-17.

In grasping to establish error in the reasoning of the District Court, appellant relies on the claim that under its interpretation of the law "all that the appellee had to do was to search the records of the county of domicile of the seller, *i. e.*, King County, Washington." <sup>18</sup> 11 Rem. Rev. Stats. of Wash. (1933), Sec. 11337-1 provides that a tax lien be recorded not in the county of domicile of the taxpayer, but in the county "within which the property subject to the lien is situated." This statute is typical of those of many states.<sup>19</sup> Thus, "the thought that if a purchaser of aircraft, such as the appellee, could not rely on the Civil Aeronautics recording system as to tax liens, he

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<sup>18</sup>Appellant's Brief, page 16.

<sup>19</sup>For example, Section 27330 of the Government Code of the State of California reads:

"§27330. Notices of liens for internal revenue taxes: Certificates of discharge. Notices of liens for internal revenue taxes payable to the United States and certificates discharging such liens may be filed in the office of the county recorder of the county *within which the property subject to the lien is situated.*"

Thus, in California as well as in Washington only one office is authorized for the recordation of federal tax liens—the recorder's office in the county in which the property is situated at the time. This is so regardless of the number of counties into which the property later passes or comes to rest. An airplane is not a stationary property. In a matter of hours it can be "situated" in a multitude of counties in numerous states. Perhaps it is a slight exaggeration to say that a purchaser of an aircraft, lacking the comforting protection derived from 49 U. S. C. 523, would have to search the recording office of *every* county of *every* state in the United States. But to be *absolutely safe and sure*, this is precisely what would have to be done. And in all events the careful buyer would be well advised to search the recording office of all counties of all states in which it was known or believed that the airplane about to be purchased had been or reasonably might have been situated. It was to correct this situation and lend stability and certainty to transactions concerning the encumbering, financing and sale of aircraft that Congress passed the statute now under attack by appellant.

might be subjected to an endless search of the records of every county in every state” is well founded in fact and not erroneous reasoning as appellant claims.

Appellant goes on to urge that in any event the District Court should not have considered the possible effect of appellant’s construction, for such a consideration was “really addressed to legislative policy.”<sup>20</sup> Legislative intent and the history and purpose of 49 U. S. C. 523 are aids to an understanding of the meaning of the statute which the courts *must* probe and weigh—not ignore as appellant argues.

“It would be anomalous to close our minds to persuasive evidence of intention on the ground that reasonable men could not differ as to the meaning of the words. Legislative materials may be without probative value, or contradictory, or ambiguous, it is true, and in such cases will not be permitted to control the customary meaning of words or overcome rules of syntax or construction found by experience to be workable; they can scarcely be deemed to be incompetent or irrelevant. See *Boston Sand & Gravel Co. v. United States*, *supra* (278 U. S. at 48, 73 L. Ed. 177, 49 S. Ct. 52). The meaning to be ascribed to an Act of Congress can only be derived from a considered weighing of every relevant aid to construction.”

*United States v. Dickerson*, 310 U. S. 554 at 562,  
84 L. Ed. 1356 at 1362.

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<sup>20</sup>Appellant’s Brief, page 16.

The following discussion by Justice Reed in *United States v. American Trucking Associations*, 310 U. S. 534 at 542-4, 84 L. Ed. 1345 at 1350-1, effectively disposes of the contention of appellant:

“In the interpretation of statutes, the function of the courts is easily stated. It is to construe the language so as to give effect to the intent of Congress. There is no invariable rule for the discovery of that intention. To take a few words from their context and with them thus isolated to attempt to determine their meaning, certainly would not contribute greatly to the discovery of the purpose of the draftsmen of a statute, particularly in a law drawn to meet many needs of a major occupation.

There is, of course, no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes. Often these words are sufficient in and of themselves to determine the purpose of the legislation. In such cases we have followed their plain meaning. When that meaning has led to absurd or futile results, however, this Court has looked beyond the words to the purpose of the act. Frequently, however, even when the plain meaning did not produce absurd results but merely an unreasonable one ‘plainly at variance with the policy of the legislation as a whole’ this Court has followed that purpose, rather than the literal words. When aid to construction of the meaning of words, as used in the statute, is available, there certainly can be no ‘rule of law’ which forbids its use, however clear the words may appear



on 'superficial examination.' The interpretation of the meaning of statutes, as applied to justicable controversies, is exclusively a judicial function. This duty requires one body of public servants, the judges, to construe the meaning of what another body, the legislators, has said. Obviously there is danger that the courts' conclusion as to legislative purpose will be unconsciously influenced by the judges' own views or by factors not considered by the enacting body. A lively appreciation of the danger is the best assurance of escape from its threat but hardly justifies an acceptance of a literal interpretation dogma which withholds from the courts available information for reaching a correct conclusion. Emphasis should be laid, too, upon the necessity for appraisal of the purposes as a whole of Congress in analyzing the meaning of clauses or sections of general acts."

It was quite fitting, therefore, if the District Court was influenced "by considerations to the effect that, if tax liens be held valid as to aircraft without being recorded with the Administrator of Civil Aeronautics, that might weaken the effectiveness and reliability of the aircraft ownership recordation system and might frustrate the purpose of Congress in establishing the central recordation system."<sup>21</sup>

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<sup>21</sup>Appellant's Brief, page 16.



### Conclusion.

The Congress of the United States in enacting 49 U. S. C. 523 recognized the peculiar problems involved in establishing the validity of a claim of title to aircraft. The language, the legislative history, and an application of fundamental rules of construction expose the intention of Congress to solve the problem by the establishment of a central office for the recordation of *all* claims to aircraft. The tenuous arguments of appellant to the contrary fail to penetrate this conclusion.

The District Court did not err in holding that 49 U. S. C. 523 establishes a system for recordation in a single agency of all claims against aircraft, including federal tax liens, and in holding that simply recording a federal tax lien under 26 U. S. C. 3672 against aircraft in the county where the aircraft may be situated at the moment is insufficient to establish the validity of a tax lien against innocent purchasers for value.

A judgment that tax liens are immune from the provisions of 49 U. S. C. 523 would require a ruling that the term "all other instruments" means nothing and was inserted in the Act by the Congress for no reason and for no purpose. That would collide with all rules of common sense and would be intolerable to the law.

The judgment of the Lower Court should be affirmed.

Respectfully submitted,

GUTHRIE, DARLING & SHATTUCK,

By HUGH W. DARLING,

*Attorneys for Appellee.*

HALE, STIMSON & RUSSELL,  
*Of Counsel.*

January 10, 1950.



No. 12347

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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UNITED STATES OF AMERICA,

*Appellant,*

*vs.*

ALL AMERICAN AIRWAYS, INC.,

*Appellee.*

On Appeal From the United States District Court for the  
Southern District of California Central Division

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## PETITION OF THE UNITED STATES FOR REHEARING.

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THERON LAMAR CAUDLE,

*Assistant Attorney General;*

ELLIS N. SLACK,

HARRY MARSELLI,

*Special Assistants to the Attorney General.*

ERNEST A. TOLIN,

*United States Attorney;*

E. H. MITCHELL,

*Assistant United States Attorney.*

600 Federal Building, Los Angeles 12,

**FILED**

MAR 17 1950

PAUL P. O'BRIEN,

CLERK



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## PETITION OF THE UNITED STATES FOR REHEARING.

---

*To the Honorable United States Court of Appeals for the  
Ninth Circuit and to the Judges Thereof:*

Comes now the United States of America, the appellant in the above entitled cause, by its attorneys, and presents this, its petition for a rehearing in the above entitled cause in which a *per curiam* opinion and judgment were rendered by this Court on February 17, 1950, and in support thereof respectfully presents the following reasons:

That this Honorable Court has erroneously assumed that the judgment appealed from by the United States is a "consent judgment" and upon the basis of that erroneous assumption has erroneously concluded to affirm the judgment of the District Court

without considering the appeal of the United States on the merits; and that in the interests of justice and fairness this Court should therefore vacate and set aside its opinion and judgment and grant a rehearing, so that it may consider the appeal of the United States on the merits, upon the points urged and argument presented by the United States.

In support hereof, the United States respectfully shows the following:

1. The *per curiam* opinion of this Court, filed in this cause on February 17, 1950, shows that the decision of this Court to affirm the judgment of the court below rests exclusively upon the assumption made by this Court that this appeal is from a "consent judgment." We submit that that assumption is so clearly erroneous, so completely without support in the record, and so contrary to the terms of the stipulation [R. 13-14], by which the parties paved the way for the entry of judgment in the court below, and to the terms of the judgment itself [R. 14-16], as well as to the obvious intent of the parties, that it would be a shocking miscarriage of justice if this Court were to permit its opinion and judgment, heretofore rendered upon the basis of that assumption, to stand.

2. This is an action brought by the appellee under 28 U. S. C., Section 2410, to quiet title to certain airplanes against which the United States had asserted liens for unpaid federal taxes due from Northern Airlines, Inc., the former owner of the airplanes. [R. 2-10.] The defendant United States moved to dismiss the action upon

the ground that the complaint failed to state a claim against the United States upon which relief could be granted. [R. 11.]

In the view of the defendant United States, the complaint alleged all of the material facts,<sup>1</sup> which the United States was willing to admit, and it did admit them, for the purpose of the motion to dismiss. In the view of the United States, the action involved only one question, upon which its only defense to the action rested, namely, a question of law as to whether the Government's otherwise valid tax lien for unpaid federal taxes due from Northern Airlines (under Section 3670 of the Internal Revenue Code), notice of which had been filed (pursuant to Section 3672(a) of the Code), was valid with respect to airplanes against a subsequent purchaser even though the tax lien had not also been "recorded" with the Administrator of Civil Aeronautics.

The United States presented its defense by a motion to dismiss, in accordance with Rule 12(b)(6) of the Federal

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<sup>1</sup>The complaint even included allegations of fact expressly made upon information furnished by the United States [Pars. VII and VIII, R. 5-7], which in the complaint is referred to as "the defendant" [R. 2-3]. Actually, the complaint was prepared upon collaboration between counsel for the appellee and for the United States so as to leave no issue of fact and as to present the question of law involved in the action in such a manner that it could be raised by a motion to dismiss. See, in this connection, the affidavit (in support of this petition) of Eugene Harpole, Esquire, one of counsel for the United States in the court below, which affidavit is submitted herewith, as an appendix hereto, and by reference made a part hereof, and the Court is respectfully requested to consider it in support of this petition.

Rules of Civil Procedure.<sup>2</sup> The motion was accompanied by a "memorandum of points and authorities in support of the motion" [R. 11] filed by the United States.<sup>3</sup> In keeping with Rule 12(d) of the Federal Rules of Civil Procedure, the motion was heard by the court below at a preliminary hearing, after which the court denied the motion without prejudice, and granted the United States 20 days within which to answer. [R. 11-12.] After the trial court had decided against the United States the question of law in the case—which, as already stated, was the *only* question in the case—further proceedings in the trial court would have been useless, and the United States thereupon determined to stand on its motion and not plead further, but to bring the question to this Court on appeal.<sup>4</sup>

In view of the decision of the United States to stand on its motion and to appeal, the parties at that point by stipulation [R. 13-14] eliminated further useless proceedings in the trial court so as to pave the way for the prompt entry by the court below—without any further, unnecessary, useless steps—of a judgment in accordance with its ruling on the motion to dismiss, from which judgment it was understood the United States would appeal.

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<sup>2</sup>This is "substantially the same as the old demurrer for failure of a pleading to state a cause of action." (Note to Subdivision (b) of Rule 12, Advisory Committee's Report of Proposed Amendments to the Federal Rules of Civil Procedure, June, 1946.) Demurrers were abolished by Rule 7(c) of the Federal Rules of Civil Procedure, which in this respect were patterned after old Equity Rule 29, which had abolished demurrers and had provided that defenses in point of law arising on the face of the bill should be made by motion to dismiss or answer. (See paragraph 3 of Note to Subdivisions (b) and (d) of Rule 12, Advisory Committee's Notes to the Federal Rules of Civil Procedure, March, 1938.)

<sup>3</sup>Additional extensive briefs were filed by both sides in the court below on the strongly contested question of law.

<sup>4</sup>See affidavit of Eugene Harpole, Appendix, *infra*.



With further steps or useless formalities so dispensed with by the stipulation of the parties, the trial court thereupon entered its judgment [R. 14-16], and the United States took its appeal [R. 17-18], exactly as contemplated and as understood by both sides. Far from being a “consent judgment,” as erroneously assumed by this Court in its *per curiam* opinion, the judgment entered by the court below was entered with the *prior* knowledge and understanding of *both* sides that the United States was not satisfied with the trial court’s decision on the question of law in the case and that the United States would appeal.

3. The mechanics which the parties chose in the court below, for the purpose of giving effect to their intention to eliminate further useless proceedings in the trial court and to pave the way for the prompt entry of a judgment from which United States could prosecute its appeal, consisted of the stipulation. [R. 13-14.] Aside from disposing of the action as to the fictitiously named defendants, the stipulation does no more than state: (1) that the United States would not plead over, *i. e.*, that it would stand on its motion to dismiss; (2) that the appellee could apply forthwith for judgment, which was approved as to form; (3) that the three-day notice required by Rule 55(b)(2) of the Federal Rules of Civil Procedure was waived; and (4) that the judgment could be entered on the allegations of the complaint, without the introduction of evidence prescribed by Rule 55(e) of the Federal Rules of Civil Procedure.

We submit that a detailed analysis of the terms of the stipulation establishes beyond the possibility of any doubt that, other than as to form and as to the procedural requirements above indicated, there was no *consent* by the United States to a judgment against it. The first para-

graph merely announces that the United States would not plead over, while the second paragraph disposes of the fictitiously named defendants, and, quite obviously, no *consent* to a judgment could possibly be "interpreted" from either of those paragraphs. The statement in paragraph three that "plaintiff may apply forthwith for judgment in the form attached hereto marked Exhibit A" [R. 13] is clearly no more than an approval *as to the form of the judgment*,<sup>5</sup> and obviously no *consent* can be implied from that. The further statement in paragraph three of the stipulation, "that the judgment may be signed and entered by the court *ex parte* and without service of a three-day written notice as provided by Rule 55(b)(2), Federal Rules of Civil Procedure" [R. 13], is clearly only a waiver of that three-day notice,<sup>6</sup> and it would be palpably wrong to construe that language as amounting to a *consent* on the part of the United States to the entry of a judgment against it, we submit.

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<sup>5</sup>Obviously, the quoted provision was put in the stipulation as a compliance with the requirements of Rule 7(a) of the Rules of the court below which, in its material part, is as follows:

All findings, conclusions of law, judgments and decrees \* \* \* shall be prepared in writing by the attorney or attorneys for the successful party \* \* \*. The counsel whose duty it is to prepare any such document shall submit a copy thereof to opposing counsel, who shall promptly (1) endorse on the original an approval, or (2) endorse a disapproval as to form \* \* \*.

That the above quoted language of the stipulation was intended as compliance with this rule of the court below is demonstrated by the fact that no endorsement as to approval appears on the judgment itself. [R. 14-16.]

<sup>6</sup>The provision of Rule 55(b)(2) calling for the notice is as follows:

If the party against whom judgment by default is sought has appeared in the action, he (or, if appearing by representative, his representative) shall be served with written notice of the application for judgment at least 3 days prior to the hearing on such application. \* \* \*

The fourth and last paragraph of the stipulation states that "the judgment may be signed and entered on the allegations in plaintiff's complaint without supporting evidence and without other or further compliance with rule 55(e), Federal Rules of Civil Procedure." [R. 14.] This, we submit, amounts to no more than a willingness on the part of the United States that the judgment be entered *on the allegations of the appellee's complaint, without the necessity of presenting the supporting evidence* which otherwise would be required by Rule 55(e) before a default judgment could be entered against the United States.<sup>7</sup> To imply a *consent* on the part of the United States to the entry of a judgment against it from paragraph four of the stipulation would require a bold disregard of the language used in the stipulation, and of the obvious intent and purpose of the stipulation in the light of the realities of the situation under which the stipulation was entered into. The United States had previously presented its only defense to the action by its motion to dismiss, under which it took the position that, admitting the facts alleged in the complaint as true, no relief could be granted as a matter of law. The trial court had denied the motion to dismiss, and the United States had decided to stand on its motion and to appeal and so, for the obvious purpose of eliminating further useless steps in the

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<sup>7</sup>Rule 55(e) provides as follows:

(e) *Judgment Against the United States.* No judgment by default shall be entered against the United States or an officer or agency thereof unless the claimant establishes his claim or right to relief by evidence satisfactory to the court.

This is substantially the same provision as was contained in the last clause of Section 763, 28 U. S. C. (action against the United States under the Tucker Act). (See note to Subdivision (e) of Rule 55, Advisory Committee's Notes to the Rules of Civil Procedure, March, 1938.)

trial court, the United States was willing to agree that the allegations of fact contained in the complaint could be taken as true and that *judgment could be entered upon them, without the necessity of having the supporting evidence introduced* as would be required by Rule 55(e). In other words, the real substance of paragraph four of the stipulation was that the United States agree that the facts pleaded in the complaint may be taken as true, and that the appellee need not establish them by proof as required by Rule 55(e).

The stipulation of the parties, when viewed in the light of the record, demonstrates unmistakably not that there was a "consent judgment" but that, after the trial court had made its decision on the question of law in the case, by its ruling on the motion to dismiss, the parties by agreement eliminated all further steps in the trial court, which would have been useless, and disposed of all procedural requirements and technicalities, so as to pave the way for the prompt entry of a judgment from which the United States could prosecute its appeal and bring the disputed question of law to this Court for decision. It would indeed be a shocking travesty on the administration of justice, we submit, if, after the United States through its attorneys had cooperated—and commendably, we feel,—with counsel for the appellee to eliminate further needless steps in the trial court so as to make possible the speedy entry of a judgment from which the United States could prosecute its appeal, this Court should deprive the United States of its right to appeal by an erroneous assumption that the judgment appealed from was a "consent judgment." It is clear from the record, we submit, that the litigation in the trial court was handled by counsel for both sides in keeping with the spirit of the Federal Rules of Civil Procedure, as stated in Rule 1, "to secure the



\* \* \* speedy, and inexpensive determination of every action.” Besides serving as a deterrent against such cooperation between counsel in the future, the decision of this Court in this case, if permitted to stand, would constitute an unjust and unwarranted deprivation of the right of the United States to appeal by erroneously assuming that the United States had *consented* to the judgment against it, whereas in fact it had merely agreed to the form of the judgment and agreed to do away with certain procedural requirements.

4. It is our position that the language of the stipulation itself establishes beyond any possible doubt that, aside from agreeing as to matters of form or procedure, the United States did not *consent* to the entry of a judgment against it. However, even if it were possible to entertain the slightest doubt under the stipulation—which we emphatically insist is impossible—such doubt would be readily dispelled by an analysis of the judgment itself. [R. 14-16.] It does not contain even the slightest suggestion that the judgment is a “consent judgment.” The preliminary or opening paragraph of the judgment [R. 14-15] merely shows that the court is deciding the case after the United States, whose motion to dismiss had been denied, had declined to plead over—*i. e.*, was standing on its motion, just as a litigant would stand on his demurrer under the old practice.

5. Clearly, there is nothing in this record which could possibly support the conclusion that there was a consent—other than as to form and procedural requirements—on the part of the United States to the entry of a judgment against it. Unless there is a *real* consent, the rule relied upon by this Court in its *per curiam* opinion, to the effect that a consent judgment is not reversible, is clearly in-



applicable, as indeed implicitly recognized by this Court in *United States v. Cushman*, 131 F. 2d 1021, in which it followed a similar holding in *Becker v. Anchor Realty & Investment Co.*, 71 F. 2d 355, 356 (C. A. 8th).

6. That there was no *real consent* on the part of the United States to the entry of judgment against it is clear beyond any doubt from the record, we believe. The only other thing which the United States could have done might have been to file some formal objection or exception to the judgment, but that, clearly, would have been futile and unnecessary. Rule 46 of the Federal Rules of Civil Procedure made formal exceptions unnecessary, it being provided in the Rule that it will be sufficient that a party make known to the court the action which he desires the court to take. See also *United States v. Barn-dollar & Crosbie*, 166 F. 2d 793, 796 (C. A. 10th).

In this case, the United States clearly and unmistakably made known to the court its position, or the action it desired the court to take: It filed a motion to dismiss the complaint for failure to state a claim upon which relief could be granted, and filed briefs (and argued orally before the court), arguing that as a matter of law the appellee was not entitled to relief because the lien of the United States for taxes was valid, when recorded in accordance with the provisions of the Internal Revenue Code, even though not "recorded" with the Administrator of Civil Aeronautics.

7. Finally, attention is invited to a further, and indeed quite significant, indication that the judgment appealed from was not a "consent" judgment. The appellee has at no time claimed that the judgment appealed from

was a "consent judgment"—neither in its brief, nor at the oral argument before the Court.<sup>8</sup>

Wherefore, in view of the foregoing, the United States respectfully requests that this, its petition for rehearing, be granted by this Honorable Court, and that the Court's *per curiam* opinion and judgment rendered and entered herein on February 17, 1950, be vacated and set aside and that a rehearing be granted and the appeal of the United States be considered on the merits.

Respectfully submitted,

THERON LAMAR CAUDLE,  
*Assistant Attorney General;*

ELLIS N. SLACK,  
HARRY MARSELLI,

*Special Assistants to the Attorney General.*

ERNEST A. TOLIN,  
*United States Attorney;*

E. H. MITCHELL,  
*Assistant United States Attorney.*

March 13, 1950.

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<sup>8</sup>No question as to whether the judgment appealed from might be a "consent judgment" was raised even by the Court at the oral argument. Aside from the merits of the appeal, the only query raised by the Court was as to whether Rule 55(e), requiring the submission of evidence before a default judgment can be entered against the United States, might not have to be complied with literally—as to which query counsel pointed out that, in substance, what had been done was the same as stipulating the facts in the case.

**Certificate of Counsel.**

The undersigned, attorneys for the United States of America, appellant in this cause, hereby certify that the foregoing petition is not presented for the purpose of delay or vexation but is, in the opinion of counsel, well founded and proper to be filed herein.

THERON LAMAR CAUDLE,  
*Assistant Attorney General;*

ELLIS N. SLACK,  
HARRY MARSELLI,

*Special Assistants to the Attorney General.*

ERNEST A. TOLIN,  
*United States Attorney;*

E. H. MITCHELL,  
*Assistant United States Attorney.*







## APPENDIX.

No. 12347

In the United States Court of Appeals for the Ninth Circuit.

United States of America, Appellant, v. All American Airways, Inc., Appellee.

AFFIDAVIT IN SUPPORT OF PETITION FOR REHEARING.

State of California, County of Los Angeles—ss:

Eugene Harpole, being first duly sworn, deposes and says: That he has been admitted to practice law in the State of Montana since June, 1922, and at all times since he has been engaged in the practice of law, and subsequently he has been admitted to the practice of law in the States of Washington and California and before the United States Court of Appeals for the Ninth Circuit and the United States District Court for the Southern District of California; that he has been an attorney employed by the Bureau of Internal Revenue since 1929, assigned to the Los Angeles office since 1931, and that he has been a Special Assistant to the Chief Counsel of the Bureau of Internal Revenue at Los Angeles since 1938. In the latter capacity he was one of the attorneys for the United States in the above entitled case when it was before the District Court of the United States for the Southern District of California.

That Robert D. Scott, an attorney admitted to practice before the courts of the State of California and before the District Court of the United States for the Southern District of California, was also a special attorney of the Bureau of Internal Revenue and the affiant's assistant at

Los Angeles, California, during the time the above-entitled case was pending before the District Court; that on November 14, 1949, Robert D. Scott resigned his position as affiant's assistant with the expressed intent of going to Addis Ababa, Ethiopia, as an advisor to the government of that nation; that affiant is informed and believes and therefore states that Robert D. Scott is now and since on and before December 1, 1949, has been in Addis Ababa, Ethiopia, and can be located at the Ras Hotel in that city.

Before the action was instituted Milo V. Olson, attorney for the plaintiff, showed the affiant a copy of the proposed complaint and as a result of conferences changes were made in the complaint to conform the allegations of fact to what affiant knew the United States would admit as true facts. As a result of the collaboration between opposing counsel in the preparation of the complaint no issue of fact remained between the parties. Accordingly, after the complaint was filed affiant caused his assistant, Robert D. Scott, to prepare a motion to dismiss which it was thought would properly raise the issue of law on which the differences between the parties rested.

On May 16, 1949, the United States District Judge Weinberger denied the defendant's motion to dismiss without prejudice and allowed 20 days to answer; on May 17, 1949, affiant's office received a notice of the ruling from Milo V. Olson (a copy of which appears at pp. 12-13 of the printed transcript of record on appeal) accompanied by a letter of transmittal (a copy of which is attached hereto, marked Exhibit A, and incorporated herein by

reference); said letter clearly expresses the intent of affiant with respect to the ruling of Judge Weinberger and reflects an understanding arrived at between affiant, Robert D. Scott, E. H. Mitchell, the assistant in the office of the United States Attorney in active charge of the case, and Milo V. Olson in discussion between them prior to the filing of the motion to dismiss.

That on May 18, 1949, a letter to the Attorney General of the United States was dictated for the signature of the United States Attorney by Robert D. Scott, with affiant's approval, and actually sent to the Attorney General, concerning the order of Judge Weinberger denying defendant's motion to dismiss. The letter contained the following paragraphs:

"Judge Weinberger on May 16, 1949, denied the Government's motion to dismiss the above entitled action, granting the defendant twenty days in which to answer or otherwise plead. Denial of the motion was without prejudice to a right to renew such motion later.

\* \* \* \* \*

"The complaint in this action was carefully worked out between counsel for the plaintiff and counsel for the Government; hence, it is believed that all material facts were properly alleged and that there would be no object in filing further pleadings or in having further trial. We recommend, therefore, (1) that we be authorized to permit judgment to be entered on the motion to dismiss, and (2) that an appeal be taken to the United States Court of Appeals for the Ninth Circuit on the ground that the Court erred in denying the Government's motion to dismiss."

On or about May 31, 1949, a teletype message was delivered to affiant's office, a copy of which is attached and marked Exhibit B and incorporated herein by reference. After the receipt of the teletype message a conference was held between the affiant, Robert D. Scott and Milo V. Olson in Mr. Scott's office, in which affiant pointed out that since it had been decided that the United States would stand upon its motion to dismiss he saw no objection in advising the District Court of that fact, namely, that the United States would file no further pleadings to plaintiff's complaint and that in order to expedite the ultimate decision in the case on appeal plaintiff need not wait the full 20 days allowed by Judge Weinberger's order of May 16, 1949, within which the defendant might answer, before applying for a judgment in its favor and that the United States would waive the requirements of Notice and Proof of the allegations of plaintiff's complaint which Rule 55(b)(2) and Rule 55(e) of the Federal Rules of Civil Procedure prescribe, and that the requirements of Rule 7(a) of the Rules of the District Court of the United States for the Southern District of California that judgments be approved as to form by counsel for the losing party could be taken care of in a stipulation.

At the close of this discussion Robert D. Scott was instructed to work out an acceptable stipulation with Milo V. Olson along the lines suggested. Within approximately 24 hours after the discussion Robert D. Scott brought the stipulation and judgment as they appear at pp. 13-16 of the printed transcript of record on appeal to affiant for



his consideration and approval. Affiant discussed the stipulation with Robert D. Scott and it was concluded between them that: (1) Since paragraph 1 of the stipulation advised the District Judge that the United States would not answer or further plead to plaintiff's complaint, the plaintiff might apply forthwith for a judgment under Judge Weinberger's order; (2) the judgment presented with the stipulation conformed to the ruling made in Judge Weinberger's order and was entitled to be approved as to form under Rule 7(a) of the District Court; (3) the provisions of Rule 55(b)(2) and (e) of the Rules of Civil Procedure requiring three-day written notice and proof of plaintiff's claim, although applicable, need not be complied with because counsel had fully collaborated in making the complaint accurate in its allegations and insistence on the letter of the rule would needlessly extend the time and labor of the litigation and needlessly enlarge the record.

As a result of the discussion the affiant signed the stipulation on behalf of the United States but (other than the approval contained in the stipulation) did not endorse "approval as to form" on the judgment, as required by Rule 7(a) of the District Court. The judgment presented to affiant with the stipulation did not recite that it was a consent judgment. Affiant had no authority or instructions in this case to consent to an entry of a judgment in plaintiff's favor and against the United States. Affiant at no time had any intention of consenting to a judgment in plaintiff's favor and against the United States; and affiant in signing the stipulation found at pp. 13 and 14



of the printed transcript of record on appeal intended not to consent to a judgment in the plaintiff's favor and against the United States, but to comply with Rule 7(a) of the Rules of the District Court and to waive if possible the requirements of Rule 55(b)(2) and (e) of the Rules of Civil Procedure, and in effect to agree that the allegations of fact in the complaint could be treated as true facts. That Affiant expressly told Milo V. Olson in the presence of Robert D. Scott, that Affiant would not and could not consent to the entry of a judgment against the United States but would merely approve the proposed judgment as to form and waive the procedural requirements just mentioned. Affiant has at all times understood the pending action to be one involving the collection of many thousands of dollars of assessed internal revenue taxes, and that it was a case of first impression, involving a seriously contested issue of law.

EUGENE HARPOLE,

Affiant.

Subscribed and Sworn to before me this 13 day of March, 1950.

(Seal)

C. M. COMMINS,

Notary Public in and for Los Angeles  
County, California.

Exhibit A.

Stanley W. Guthrie  
Hugh W. Darling  
Edward S. Shattuck  
Milo V. Olson  
Arthur C. Jones, Jr.  
George G. Gute

Trinity 8104

Law Offices  
GUTHRIE, DARLING & SHATTUCK  
737 Pacific Mutual Building  
Los Angeles 14

May 16, 1949.

Mr. Eugene Harpole  
Mr. Robert D. Scott  
Bureau of Internal Revenue  
1727 Federal Building  
Los Angeles 12, California.

Gentlemen:

All American v. U. S.

Enclosed is a notice of ruling. I understand the defendant will not answer but will take an appeal.

Cordially,

MILO V. OLSON,  
MILO V. OLSON,  
of

GUTHRIE, DARLING & SHATTUCK.

MVO:r

Exhibit B.

TELETYPE UNIT

MAY 31 AM 8:19

PUBLIC BLDGS. ADM.

LOS ANGELES

T

402 LA WAY J-D

WASHINGTON DC 5-31-49 1114A

CARTER UNITED STATES ATTORNEY

LA

RE ALL AMERICAN AIRWAYS INC VERSUS UNITED STATES  
NUMBER 8860-WC YOUR REFERENCE EHM/EH/RDS/MRK LET  
JUDGMENT BE ENTERED ON GOVERNMENTS MOTION TO DIS-  
MISS. ADVICE CONCERNING ATTORNEY GENERALS DECISION  
ON QUESTION OF APPEAL WILL BE FORWARDED ON AN  
EARLY DATE.

CAUDLE ASSISTANT ATTORNEY GENERAL JUSTICE DE-  
PARTMENT

8860-WC

RR 1116A

Nos. 12,349 and 12,352

IN THE  
United States Court of Appeals  
For the Ninth Circuit

TIMOTHY E. ARMSTRONG, et al.,  
*Appellants,*

vs.

MATSON NAVIGATION COMPANY (a corporation), and UNITED STATES OF AMERICA,  
*Appellees.*

No. 12,349

(CONSOLIDATED  
CASES)

JAMES KEITH CURRIE, as Administrator of the Estate of Jack George Currie, Deceased,  
*Appellant,*

MATSON NAVIGATION COMPANY (a corporation), and UNITED STATES OF AMERICA,  
*Appellees.*

No. 12,352

APPELLANTS' PETITION TO MODIFY OR AMEND DECISIONS.

ALBERT MICHELSON,  
Russ Building, San Francisco 4,  
*Proctor for Appellants  
and Petitioners.*

HERBERT CHAMBERLIN,  
Russ Building, San Francisco 4,  
*Of Counsel.*





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Nos. 12,349 and 12,352

IN THE

# United States Court of Appeals

For the Ninth Circuit

TIMOTHY E. ARMSTRONG, et al.,  
*Appellants,*

vs.

MATSON NAVIGATION COMPANY (a corporation), and UNITED STATES OF AMERICA,  
*Appellees.*

No. 12,349

JAMES KEITH CURRIE, as Administrator of the Estate of Jack George Currie, Deceased,

*Appellant,*

vs.

MATSON NAVIGATION COMPANY (a corporation), and UNITED STATES OF AMERICA,  
*Appellees.*

(CONSOLIDATED  
CASES)

No. 12,352

APPELLANTS' PETITION TO MODIFY OR AMEND DECISIONS.

*To the Honorable United States Court of Appeals for the Ninth Circuit, and to the Honorable Clifton Mathews, William E. Orr, and Walter C. Lindley (sitting by special designation), Circuit Judges:*

The appellants in the above entitled and consolidated causes respectfully petition for the modification or amendment of the decisions therein, as follows:

That the decision in each cause be modified or amended to provide that the cause be remanded to the District Court for the entry of a decree for each appellant determining for each the amount of war bonus to which he is entitled, with interest and costs, pursuant to the opinion of this court rendered July 18, 1950.

The decisions herein followed the decisions of the same court in the President Harrison cases (*Agnew v. American President Lines*, 9 Cir. 1949, 177 F. 2d 107; *Federer v. American President Lines*, 9 Cir. 1949, 177 F. 2d 111; *Griffin v. American President Lines*, 9 Cir. 1949, 177 F. 2d 111; Cert. den. 339 U.S. 951). In each of those cases the cause was remanded to the District Court "for the entry of a decree for each appellant determining for each the amount of war bonus to which he is entitled pursuant to the above opinion" with interest and costs. (177 F. 2d 110, 111, 113-114.) A speedy, final, and just disposition of each cause was thereby accomplished in accord with approved admiralty practice and procedure. (*Menefee v. W. R. Chamberlin Co.*, 9 Cir. 1949, 176

F. 2d 828.) The same result will be accomplished, and the precedent of the President Harrison cases followed, if the modification or amendment here sought by petitioners is granted.

Wherefore your petitioners respectfully pray that the decisions in the above entitled and consolidated causes be modified or amended in the foregoing respect and particular.

Dated, San Francisco,  
August 16, 1950.

ALBERT MICHELSON,  
*Proctor for Appellants  
and Petitioners.*

HERBERT CHAMBERLIN,  
*Of Counsel.*





### CERTIFICATE OF PROCTOR

I hereby certify that I am proctor for appellants and petitioners in the above entitled and consolidated causes and that in my judgment the foregoing petition is well founded in point of law as well as in fact and that said petition is not interposed for delay.

Dated, San Francisco,  
August 16, 1950.

ALBERT MICHELSON,  
*Proctor for Appellants  
and Petitioners.*









Nos. 12,349, 12,352, 12,350

# In the United States Court of Appeals

## For the Ninth Circuit

TIMOTHY E. ARMSTRONG, et al., *Appellants,*  
vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

**No. 12,349**

JAMES KEITH CURRIE, etc., *Appellant,*  
vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

**No. 12,352 CONSOLIDATED  
CASES**

DONALD G. STEWART, et al., *Appellants,*  
vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

**No. 12,350**

## Petition for Modification of Opinion

*To the Judges of the United States Court of Appeals for  
the Ninth Circuit:*

MATSON NAVIGATION COMPANY, appellee and cross-appellant herein (hereinafter referred to as "Matson"), respectfully requests that the Court modify its opinion filed on

July 18, 1950. It is specifically requested that this Court pass upon the cross-appeals of Matson and that the opinion be amended so as to remand the case to the District Court for such further proceedings as may be advisable in connection with the determination of the liability of the United States of America to Matson.

As indicated in the brief originally filed herein on behalf of Matson, it, at the time that it answered the libels, impleaded the United States of America as a party respondent based upon the charter party provisions whereby the United States agreed to indemnify Matson for certain items including war bonuses and maintenance claims. The United States, in its answers to the impleading petitions, admitted that as between it and Matson, it was liable to reimburse Matson for its actual out-of-pocket expenses for any war bonuses. Because of the fact that the trial court held that the libelants were not entitled to recover anything from Matson, this subsidiary question of the liability of the United States became moot. However, in order to protect its rights in the event of a reversal by this Court, Matson took cross-appeals from the final decree adjudging that it recover nothing from the United States either on the bonus claims or on the maintenance claims.

This Court has now reversed the District Court on the bonus claims and has affirmed the District Court on the maintenance claims. We are not challenging the decision of this Court on these issues, but we respectfully point out that the opinion of this Court makes no mention whatever of the cross-appeals taken by Matson and there is therefore left completely undecided the question of the liability of the United States to Matson for the amounts which Matson will be compelled to pay to the libelants.

The Statement of the Case and Argument in connection with this matter are completely covered in Matson's original brief, pages 6 to 9, inclusive, and it seems unnecessary at this time to repeat any of the material contained therein. However, we do point out that if the opinion is not amended, Matson may find itself in the position that when the Mandate of this Court goes down to the District Court, the latter Court might feel that it has no jurisdiction to pass upon the question of the liability of the United States to Matson.

Accordingly, it is respectfully requested that this Court pass upon the cross-appeals of Matson and that it modify its opinion so as to remand the case to the District Court for such further proceedings as may be advisable in connection with the determination of the liability of the United States to Matson based upon the impleading petitions.

Respectfully submitted,

BROBECK, PHLEGER & HARRISON,  
ALAN B. ALDWELL,

*Proctors for Appellee and  
Cross-Appellant Matson  
Navigation Company.*

Dated at San Francisco, California,  
August 17, 1950.



Nos. 12,349 and 12,352

IN THE

United States Court of Appeals

For the Ninth Circuit

TIMOTHY E. ARMSTRONG, WILLIAM J. CONNOLLY, FILBERT DE LA ROSA, ERNEST DE LIMA, DAVID F. DONNELLY, LEON D. DUPUICH, STANLEY F. FISKE, LOUIS R. HICKSON, GUY T. HOUSTON, PAUL R. HOWLE, EMIL JOHNSON, THEODORE KALLEGAS, JOSEPH MARCUS, JOHN E. MORRIS, PAULUS OLSEN, NICANOR PENNA, JULIUS PIECHURA, GORDON POLLARD, LEONARD K. POWERS, ALBERT RIIS, DONALD SMITH, JAMES V. STINGLEY, HAROLD D. VALLIER, and KEITH M. WESTDYKE,

*Appellants,*

vs.

MATSON NAVIGATION COMPANY (a corporation), and UNITED STATES OF AMERICA,

*Appellees.*

No. 12,349

(CONSOLIDATED  
CASES)

JAMES KEITH CURRIE, as Administrator of the Estate of JACK GEORGE CURRIE, Deceased,

*Appellant,*

vs.

MATSON NAVIGATION COMPANY (a corporation), and UNITED STATES OF AMERICA,

*Appellees.*

No. 12,352

FILED

OCT 11 1941

BRIEF FOR APPELLANTS.

PAUL P. O'BRIEN,

ALBERT MICHELSON,

Russ Building, San Francisco 4,

*Proctor for Appellants.*





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Nos. 12,349 and 12,352

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

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TIMOTHY E. ARMSTRONG, WILLIAM J.  
CONNOLLY, FILBERT DE LA ROSA,  
ERNEST DE LIMA, DAVID F. DON-  
NELLY, LEON D. DUPUICH, STANLEY  
F. FISKE, LOUIS R. HICKSON, GUY T.  
HOUSTON, PAUL R. HOWLE, EMIL  
JOHNSON, THEODORE KALLEGAS, JO-  
SEPH MARCUS, JOHN E. MORRIS,  
PAULUS OLSEN, NICANOR PENA,  
JULIUS PIECHURA, GORDON POLLARD,  
LEONARD K. POWERS, ALBERT RIIS,  
DONALD SMITH, JAMES V. STINGLEY,  
HAROLD D. VALLIER, and KEITH M.  
WESTDYKE,

*Appellants,*

vs.

MATSON NAVIGATION COMPANY (a cor-  
poration), and UNITED STATES OF  
AMERICA,

*Appellees.*

No. 12,349

(CONSOLIDATED  
CASES)

JAMES KEITH CURRIE, as Administrator  
of the Estate of JACK GEORGE CUR-  
RIE, Deceased,

*Appellant,*

vs.

MATSON NAVIGATION COMPANY (a cor-  
poration), and UNITED STATES OF  
AMERICA,

*Appellees.*

No. 12,352

**BRIEF FOR APPELLANTS.**

**FOREWORD.**

These cases are two of four cases consolidated for trial and now before this court on appeal as Nos. 12349, 12350, 12351, and 12352.

In case No. 12349 the libelants were seamen seeking recovery of bonus wages and maintenance for the time they were interned by the Japanese and in war zone areas. In case No. 12352 the libelant was an administrator seeking recovery of similar bonus wages and maintenance of a deceased seaman. The term "libelant" or "libelants" as used in subsequent parts of the brief is intended to include this deceased seaman unless otherwise indicated.

When the libels were originally filed the sole respondent was appellee Matson Navigation Company. (A 1.) It impleaded United States of America as respondent because of charter party agreement, dated November 24, 1941, stipulating certain reimbursement and indemnity in favor of respondent Matson Navigation Company. (A 27-30.) The libelants have no concern with this charter party on their appeal. The term "respondent" or "appellee" as used in subsequent parts of the brief is intended to apply to respondent and appellee Matson Navigation Company.

The two cases have a record largely in common, and an order of this court was heretofore made consolidating them on appeal, dispensing with formal Apostles in No. 12352, and permitting a common brief. References herein are to the Apostles in the Armstrong case (No. 12349). Matters peculiar to the Currie

case (No. 12352) and showing the timeliness and regularity of the appeal therein are included in the Appendix to the brief.

The trial judge decided these cases adversely to the libelants on the authority of his earlier decision in *Agnew v. American President Lines, Ltd.* (The *President Harrison*), 73 F. Supp. 944. (A 82.) With slight exceptions, the present cases parallel the cases before the court in *Agnew v. American President Lines, Ltd.*, No. 11943, and *Griffin v. American President Lines, Ltd.*, No. 11944, reversing 73 F. Supp. 944, as to the claims for bonus wages and affirming it as to the claims for maintenance.

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#### STATEMENT OF JURISDICTION.

The libel in No. 12349 was in admiralty by seamen to recover wages and maintenance. (A 1-8.) The libel in No. 12352 was in admiralty by an administrator to recover wages and maintenance of a deceased seaman. (A 84-97.) The District Court had jurisdiction. (28 U.S.C.A., sec. 41 (3), now 28 U.S.C.A. Judiciary and Judicial Procedure, sec. 1333.) Final decree in both actions was entered March 24, 1949. (A 99-101.) Notice of Appeal in both actions was filed June 20, 1949. (A 109-110; Appx., Notice of Appeal.) An order allowing appeal was entered the same day. (A 106; Appx., Order Allowing Appeal.) The appeals were timely taken (28 U.S.C.A. Judiciary and Judicial Procedure, sec. 2107) and timely docketed (A 128-129;

Appx., Order Extending Time). Jurisdiction of this court to review the final decree of the District Court is therefore sustained by 28 U.S.C.A. Judiciary and Judicial Procedure, secs. 1291, 1294.

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### **STATEMENT OF THE CASE.**

The libelants were members of the licensed and unlicensed personnel of the crew of respondent's ship MALAMA when it sailed from San Francisco for the Philippine Islands on November 29, 1941. (A 87-88.)

For the deck, the licensed personnel were members of the National Organization of Masters, Mates and Pilots of America. (A 89-91.) In case No. 12349, licensed personnel in that class were libelants Leon D. Dupuich, Gordon Pollard, and Keith M. Westdyke. (A 89-90.) And for the deck, the unlicensed personnel were members of the Sailors' Union of the Pacific. (A 89-91.) In case No. 12349, unlicensed personnel in that class were libelants Timothy E. Armstrong, Ernest De Lima, Stanley F. Fiske, Guy T. Houston, Emil Johnson, Joseph Marcus, Paul Olsen, Julius Piechura, Albert Riis; and in case No. 12352, Jack George Currie. (A 89-90.)

For the engine room, the licensed personnel were members of the Marine Engineers' Beneficial Association. (A 89-91.) In case No. 12349, licensed personnel in that class were libelants William J. Connolly, Filbert De La Rosa, Louis R. Hickson, and Donald Smith. (A 89-90.) And for the engine room, the unlicensed



personnel were members of the Pacific Coast Marine Firemen, Oilers, Watertenders and Wipers' Association. (A 89-90.) In case No. 12349, unlicensed personnel in that class were libelants David D. Donnelly, Paul R. Howle, Theodore Kallegas, John E. Morris, Nicanor Pena, Leanard K. Powers, James V. Stingley, and Harold D. Vallier. (A. 89-90.)

The MALAMA arrived at Honolulu December 8, 1941—the day after the Japanese bombed Pearl Harbor. (A 88.) Eight days later the ship sailed *for New Zealand*. (A 88.) On January 1, 1942, the ship was sunk by enemy action of the Japanese about 600 miles southeast of Tahiti, and the crew made prisoners of war. (A 88.) For the next 42 days they were on a Japanese raider enroute to Japan, crossing the 180th meridian westbound on January 6, 1942. (A 88.) Thereafter, and for the duration of the war, they were interned by the Japanese west of the 180th meridian. (A 88.) They were liberated about September 5, 1945, and on repatriation recrossed the 180th meridian eastbound on the various dates set forth in respondent's answer (A 21-22) and stipulated to at the trial. Libelants received no maintenance from respondent, or payment therefor, subsequent to January 1, 1942.

The photostatic copy of the shipping articles of the MALAMA admitted in evidence at the trial as Libelants' Exhibit No. 2, is on file in this court. The following rider *applicable to licensed personnel* was part of the shipping articles:



### “RIDER

“The Matson Navigation Company agrees to pay war risk bonuses to the crew of the SS MALAMA from the crossing of the 180th Meridian Westbound until recrossing the same Meridian Eastbound as follows:

LICENSED DECK OFFICERS:  $66\frac{2}{3}\%$  of the basic monthly wages effective as of Oct. 1, 1941;

LICENSED ENGINE OFFICERS:  $66\frac{2}{3}\%$  of the basic monthly wages effective as of Oct. 1, 1941;

RADIO OFFICER:  $66\frac{2}{3}\%$  of the basic monthly wage effective as of Oct. 1, 1941.

“In the event the vessel is ordered by an Agency or Department of the United States Government to return via another trade route, war risk bonuses will be paid while the vessel is in any of the war zone areas I to VI inclusive at the rates described in the supplementary agreements between the various Marine Unions and the Pacific American Shipowners Association of San Francisco.

“In the event of loss of personal effects by any Licensed Deck Officer, Licensed Engine Officer, or radio Officer, due to the necessity of the abandoning ship resulting from torpedoing, mining or bombing of the vessel, each such officer so affected shall be reimbursed by a sum not to exceed \$500.00.

“In the event the vessel be interned, destroyed or abandoned as a result of war operations and be unable to continue her voyage, basic wages and emergency wages specified in the collective bargaining agreements between the parties shall be

paid to the date members of the crew arrive in Continental United States ports and the employes shall be repatriated to a Continental United States port. While employes are in the war zone areas described in the supplementary agreements covering war risk bonuses payable to Licensed Officers, war risk bonuses shall also be paid to them at the rate of  $66\frac{2}{3}\%$  of the said basic wages in Areas I to V inclusive, and 25% in Area VI.

“War Risk Insurance shall be furnished each Licensed Officer of the SS MALAMA, Voy. No. 54, for the voyage as described on ship’s Articles; such policy shall provide for the payment of the said sum of \$5,000.00 to the estate or designated beneficiary of such Licensed Officer in case of death due to war conditions or the payment of said sum to the Licensed Officer himself in the event of his total and permanent disability due to such war conditions, and shall provide for the payment of any sum less than \$5,000.00 to which such Licensed Officer may be entitled for injury less than total or permanent disability resulting from said war conditions. Such policies shall be made available for inspection at the office of the Company.

“(Initialed JJb)”

And the following rider applicable to *unlicensed personnel* was also part of the shipping articles:

#### “RIDER

“The Matson Navigation Company agrees to pay war risk bonuses to the crew of the SS MALAMA from the crossing of the 180th Meridian Westbound until recrossing the same Meridian Eastbound, as follows:

“UNLICENSED DECK PERSONNEL: \$80.00 per month;  
UNLICENSED ENGINE PERSONNEL: \$80.00 per month;

STEWARD'S PERSONNEL: \$80.00 per month to all employees entitled to receive \$120.00 or less as basic monthly wages as of Oct. 1, 1941; 66 $\frac{2}{3}$ % of the basic monthly wages in excess of \$120.00.

“In the event the vessel is ordered by an Agency or Department of the United States Government to return via another trade route, war risk bonuses will be paid while the vessel is in any of the war zone Areas I to VI inclusive at the rates prescribed in the supplementary agreements between the various Marine Unions and the Pacific American Shipowners Association at San Francisco.

“In the event of loss of personal effects by any unlicensed member of the crew, due to the necessity of abandoning ship resulting from torpedoing, mining or bombing of the vessel, the company agrees to reimburse each unlicensed man so affected by an amount not in excess of \$150.00.

“In the event the vessel be interned, destroyed or abandoned as a result of war operations and is unable to continue her voyage, basic wages and emergency wages specified in the collective bargaining agreements between the parties shall be paid to the date the members of the crew arrive in a Continental United States Port, and the employees shall be repatriated to a Continental United States Port. War risk bonuses at the rates specified in sub-division (b) paragraph 1 of the supplementary agreements between the parties shall

be paid while employes are in the war zone areas defined therein.

“War Risk Insurance in the sum of \$5,000.00 shall be furnished to each member of the crew of the SS MALAMA, Voy. No. 54, for the voyage as described on Ship’s Articles.

“(Initialed JJB)”

Each libelant in case No. 12349 sought to recover war bonus at the appropriate rate stipulated in the applicable rider covering the period from the crossing of the 180th meridian westbound until crossing the same meridian eastbound. (A 4-5.) Each said libelant also sought to recover maintenance from date of capture by the Japanese on January 1, 1942, to date of liberation on September 5, 1945. (A 5.) The claim of each libelant was computed in a schedule annexed to the libel. (A 7-8.) Each said libelant further sought to recover interest and costs. (A 6.) Similar claims were made in case No. 12352 respecting the deceased seaman.

The District Court found that the shipping articles did not entitle libelants to the war bonus they claimed. (A 93-95.) It further found that libelants were not entitled to the maintenance they claimed. (A 95.) Its final decree was that “the libelants have and recover nothing from the respondent or the impleaded respondent herein and that such libels be dismissed”. (A 101.)

One of the broad grounds on appeal is that the shipping articles clearly entitled libelants to the war bonus



they claimed and that the findings and judgment against them in such respect are contrary to the evidence and the law. Another broad ground on appeal is that the general maritime law clearly entitled libelants to the maintenance they claimed and that the findings and judgment against them in such respect are contrary to the evidence and the law.

Rulings of the trial court respecting evidence are also assigned as error. One ruling excluded evidence of the construction given the shipping articles by the parties at the time of signing. (A 111; Appx., Assignment of Errors.) Another ruling excluded evidence of contemporaneous oral contract between the parties for payment of war bonus for period of internment on land. (A 111; Appx., Assignment of Errors.) And still another ruling excluded evidence of deviation of voyage. (A 111-112; Appx., Assignment of Errors.)

After the submission of the cases, libelants moved to set aside the submission and reopen the causes for further proof, namely, testimony of the master of the MALAMA when the shipping articles were signed. (A 68-70.) The motion was supported, in part, by his affidavit, explaining his absence from continental United States at the time of trial, and averring that in his presence the Deputy Shipping Commissioner told the seamen, in response to their inquiries as to the meaning of the riders, that if the vessel was captured or interned their wages and bonus would go on until they got back to the United States, and that affiant, as master of the vessel, said nothing, for the reason that he had the same understanding as to the



meaning of the riders. (A 71-72.) The denial of this motion is assigned as error. (A 112; Appx., Assignment of Errors.)

Appellants ask that the final decree of the District Court be reversed and the causes remanded for the entry of a decree for each appellant determining for each the amount of war bonus and maintenance to which he is entitled, with interest at 7% per annum from the date his libel was filed, and costs.

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#### **SPECIFICATION OF ASSIGNED ERRORS RELIED UPON.**

The assigned errors are the same in each case except to the extent that an administrator-libelant in case No. 12352 required change in phraseology. Each appellant relies upon each of his assigned errors, namely, Nos. 1 to 12, both inclusive. (A 111-113; Appx., Assignment of Errors.)

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#### **ARGUMENT OF THE CASE.**

1. **THE SHIPPING ARTICLES WERE PLAIN, CERTAIN, AND UNAMBIGUOUS, AND CLEARLY ENTITLED THE LIBELANTS TO WAR BONUS, AT THE RATES STIPULATED THEREIN, COVERING THE PERIOD FROM THE CROSSING OF THE 180TH MERIDIAN WESTBOUND UNTIL CROSSING THE SAME MERIDIAN EASTBOUND.**

*Assignment of Error No. 1:* "The court erred in decreeing that libelants have and recover nothing from the respondent or the impleaded respondent." (A 111; Appx., Assignment of Errors.)

*Assignment of Error No. 2:* "The court erred in decreeing that the libel be dismissed." (A 111; Appx., Assignment of Errors.)

*Assignment of Error No. 8:* "The court erred in finding that the riders attached to the shipping articles were ambiguous, vague, or uncertain." (A 112, Appx., Assignment of Errors.)

*Assignment of Error No. 9:* "The court erred in finding that libelants were not and each libelant was not entitled to war bonus for the period of internment on land west of the 180th meridian." (A 112; Appx., Assignment of Errors.)

*Assignment of Error No. 10:* "The court erred in failing to find and decree that libelants were and each libelant was entitled to war bonus, at the rate specified in the shipping articles, for the period of internment on land west of the 180th meridian, together with interest thereon." (A 112; Appx., Assignment of Errors.)

In denying the claims of libelants for war bonus the District Court merely followed its earlier decision in the President Harrison cases, *Agnew v. American President Lines, Ltd.*, 73 F. Supp. 944. (A 82.) But the decision of the District Court in the President Harrison cases insofar as it denied the libelants war bonus was reversed by this court in *Agnew v. American President Lines, Ltd.*, No. 11943, *Griffin v. American President Lines, Ltd.*, No. 11944, and *Federer v. American President Lines, Ltd.*, No. 11946. In those cases this court definitely decided that shipping article

riders worded as those here involved entitled captured and interned seamen to war bonus from the time they crossed the 180th meridian westbound until they recrossed the same meridian eastbound. It would be idle for appellants to do more than invoke the authority of those decisions to demonstrate that the final decree herein denying war bonus should be reversed and a decree entered for war bonus as claimed by libelants.

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**2. THE COURT ERRED IN EXCLUDING EVIDENCE OF THE CONSTRUCTION GIVEN THE SHIPPING ARTICLES BY THE PARTIES AT THE TIME OF SIGNING. (Assignment of Error No. 4.) (A 111; Appx., Assignment of Errors.)**

The shipping articles, signed in 1941, reflected an agreement between the master and the seamen. (45 U.S.C.A., sec. 564.) In employing seamen the master acted as the agent of respondent and his principal was bound by his acts, admissions, conduct, and knowledge. (*Butler v. Boston etc. Co.*, 139 U.S. 527, 9 S. Ct. 612, 616, 32 L. Ed. 1017.) The master was subject to superintendence by the shipping commissioner. (46 U.S.C.A., sec. 545.) Before the shipping articles were signed, it was the duty of the shipping commissioner to acquaint master and seamen with the conditions thereof and to ascertain that they understood the same. (45 U.S.C.A., sec. 565.)

The libelants produced Leon Dupuich as a witness at the trial. (A No. 12351, Vol. II, p. 6.) He was second officer of the MALAMA. (A 89.) When interrogated concerning what occurred when the shipping articles

were signed in the presence of a Deputy Shipping Commissioner and the master, he replied that the shipping commissioner told the seamen in response to their inquiries as to what the riders meant that they would be paid wages and bonus "until they were repatriated to a continental United States port". (A 12351, Vol. II, p. 16.) A motion to strike this testimony was granted. The court erred. The construction given a contract by the parties is always a consideration of great weight, is usually adopted by the courts, and evidence thereof is competent. (*Brooklyn Life Ins. Co. v. Dutcher*, 96 U.S. 269, 273, 24 L. Ed. 410; *United States v. Johnson*, 9 Cir. 160 F. 2d 326, 329.)

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3. **THE COURT ERRED IN EXCLUDING EVIDENCE OF CONTEMPORANEOUS ORAL CONTRACT BETWEEN THE PARTIES FOR PAYMENT OF WAR BONUS FOR PERIOD OF INTERNMENT ON LAND.** (Assignment of Error No. 5.) (A 111; Appx., Assignment of Errors.)

Under the theory entertained by the trial court that neither the shipping articles nor the collective bargaining agreements stipulated for payment of war bonus while the seamen were interned on land (*Agnew v. American President Lines, Ltd.*, 73 F. Supp. 944), it was obvious error for the court to exclude the evidence just mentioned, for such evidence would be competent to establish a contemporaneous oral agreement covering such contingency (*Dittmar v. Star Cont. Co.*, 2 Cir., 249 F. 437, 438; *The Lola*, Fed. Cas. No. 8468; 3 Williston, Contracts 1832-1835,



1842, secs. 637-638, 642). The theory of the court was wrong, of course, and error will disappear when this court declares the theory wrong.

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4. **THE COURT ERRED IN EXCLUDING EVIDENCE OF DEVIATION OF VOYAGE.** (Assignment of Error No. 6.) (A 111-112; Appx., Assignment of Errors.)

The evidence at the trial established that the MALAMA sailed from San Francisco November 29, 1941, arrived in Honolulu December 8, 1941, sailed from Honolulu for New Zealand 8 days later, and was sunk by enemy action of the Japanese and the crew made prisoners of war on January 1, 1942, 600 miles southeast of Tahiti. (A 88.) At the trial libelants offered evidence that deviation of voyage had occurred. (A No. 12541, Vol. II, pp. 17-18.) The court held such evidence inadmissible and granted motions to strike it, (A 36.) This was error.

The shipping articles, entered into before the outbreak of the war with Japan, stipulated for a voyage from the port of San Francisco to the Philippine Islands and back to a final Pacific Coast port of discharge. That a voyage to New Zealand after the outbreak of the war was a deviation from the stipulated voyage cannot be questioned. (*The Chester Valley*, 5 Cir., 110 F. 2d 592, 594; *The Pelotas*, 5 Cir., 66 F. 2d 75, 77; *General Hide & Skin Corp. v. United States*, D.C. N.Y. 24 F. 2d 736, 738; *The Henry W. Cramp*, 3 Cir., 20 F. 2d 320, 321; *Shackman v. Cunard White Star*, D.C. N.Y. 31 F. Supp. 948, 951.)



Speculation as to whether it was safer after the outbreak of war to send the ship and crew on a voyage to New Zealand instead of the Philippine Islands, or as to whether it would have been safer to return them to San Francisco, is wholly immaterial. What is material is that there was a deviation from the voyage stipulated in the shipping articles, and that a different voyage, without the signing of new shipping articles, was undertaken after war with Japan had created hazardous conditions which did not exist when shipping articles were signed at San Francisco. The law addressed to analogous situations has declared that under such circumstances these seamen were entitled to the fullest measure of compensation, including maintenance, until their return to the United States. (*Sheppard v. Taylor*, 30 U.S. 675, 8 L. Ed. 268, 282; *The Kentra*, D.C. N.Y. 286 F. 163; *Turtle v. Northwestern SS Co.*, D.C. Wash., 154 F. 146, affirmed *Northwestern SS Co. v. Turtle*, 9 Cir., 162 F. 256.)

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5. **THE COURT ERRED IN DENYING THE MOTION OF LIBELANTS TO SET ASIDE THE SUBMISSION AND REOPEN CAUSE FOR INTRODUCTION OF FURTHER PROOF.** (Assignment of Error No. 7.) (A 112; Appx., Assignment of Errors.)

After the submission of the cases, libelants moved to set aside the submission and reopen the causes for further proof, namely, testimony of the master of the MALAMA when the shipping articles were signed. (A 68-70.) An affidavit in support of the motion was made by master, explaining his absence from conti-

mental United States at the time of trial, and averring that in his presence the Deputy Commissioner told the seamen, in response to their inquiries as to the meaning of the riders, that if the vessel was captured or interned their wages and bonus would go on until they got back to the United States, and that affiant, as master of the vessel, said nothing, for the reason that he had the same understanding as to the meaning of the riders. (A 71-72.) The motion was denied, it being recited in the order that "it be deemed that said Malcolm R. Peters has testified in said causes in accordance with his affidavit annexed to said motion and that such testimony was thereafter stricken as inadmissible the same as if a motion to strike said testimony had been made and granted". (A 79.)

The court erred in denying the motion. A submission should be set aside and a cause reopened for the introduction of further testimony in furtherance of justice. (*The Bainbridge*, 9 Cir., 199 F. 404, 409; *De Sousa v. Dollar S. S. Lines*, D.C. Wash., 292 F. 490, 491.) The master was the agent of the shipowner, and the shipowner was bound by his knowledge, acts, conduct, and admissions in the employment of the crew. (*Butler v. Boston etc. Co.*, 130 U.S. 527, 9 S. Ct. 612, 618, 32 L. Ed. 1017; *Andrews v. Wall*, 44 U.S. 568, 11 L. Ed. 729, 731; *United States v. Gooding*, 25 U.S. 460, 6 L. Ed. 693, 696.) The proposed testimony of Captain Peters was competent and decisively in favor of libelants on the issue then before the court as to the period for which the seamen were entitled to war bonus. (*Brooklyn Life Ins. Co. v. Dutcher*, 95 U.S. 269,

273, 24 L. Ed. 410; *United States v. Johnson*, 9 Cir., 160 F. 2d 769, 797; *International Co. v. Sloan*, 10 Cir., 114 F. 2d 326, 329; 3 Williston, Contracts 1792-1795, sec. 632.)

It is now obvious of course that the shipping commissioner and the master interpreted the riders to the Malama shipping articles in accord with the interpretation given by this court to similar riders in the President Harrison cases. This claim of error becomes academic when the rule of those cases is followed, but it was error and prejudicially so when the District Court was following a contrary rule.

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**6. THE DISTRICT COURT ERRED IN DENYING LIBELANTS ANY RECOVERY OF MAINTENANCE.**

*Assignment of Error No. 11:* "The court erred in finding that libelants were not and each libelant was not entitled to maintenance after January 1, 1942." (A 112; Appx., Assignment of Errors.)

*Assignment of Error No. 12:* "The court erred in failing to find and decree that libelants were and each libelant was entitled to maintenance after January 1, 1942, and to payment therefor and to interest thereon." (A 112-113; Appx., Assignment of Errors.)

In the President Harrison cases this court affirmed the decree of the District Court (73 F. Supp. 944) insofar as it denied maintenance claims of the libelants. The appellee therein has indicated an intention to petition the Supreme Court for certiorari and, if

granted, it is possible that the question of maintenance will be reopened. These appellants therefore wish to keep the question open here and the reasons advanced in the President Harrison cases for the allowance of maintenance are therefore reurged. Moreover, additional and cogent reason for the allowance of maintenance exists in the Malama cases. Deviation of voyage is involved. Where deviation of voyage has occurred seamen are entitled to the fullest measure of compensation, *including allowance for maintenance*, until they get back to a home port. (*Sheppard v. Taylor*, 30 U.S. 675, 8 L. Ed. 268, 282; *The Kentra*, D.C. N.Y. 286 F. 163; *Turtle v. Northwestern SS Co.*, D.C. Wash., 154 F. 146, affirmed *Northwestern SS Co. v. Turtle*, 9 Cir., 162 F. 256.) Appellants invoke that rule.

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#### 7. LIBELANTS ARE ENTITLED TO INTEREST AND COSTS.

Assignment of Error No. 10, earlier quoted, challenged as error the failure of the court to decree war bonus, "together with interest thereon". (A 112; Appx., Assignment of Errors.) Assignment of Error No. 12, earlier quoted, challenged as error the failure of the court to decree maintenance, and "interest thereon". (A 112-113; Appx., Assignment of Errors.) In support of these assignments it is enough to cite the decisions of this court in the President Harrison cases allowing interest and costs.

**CONCLUSION.**

Appellants therefore respectfully submit that the decree of the District Court should be reversed with directions to the court to award libelants (1) war bonus from the time they crossed the 180th meridian westbound until they recrossed the same meridian eastbound, (2) maintenance for the period of their internment, (3) interest thereon, at 7% per annum from date of filing libel, and (4) costs.

Dated, San Francisco,  
October 24, 1949.

ALBERT MICHELSON,  
*Proctor for Appellants.*

**(Appendix Follows.)**







## Appendix

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Original filed June 21, 1949,

Clerk, U. S. Dist. Court, San Francisco.

In the United States District Court for the Northern  
District of California, Southern Division

In Admiralty  
No. 24,807-H-G

James Keith Currie, as Administrator  
of the Estate of Jack George Currie,  
Deceased,

Libelant,

vs.

Matson Navigation Company (a cor-  
poration),

Respondent,

United States of America,

Impleaded Respondent.

### ASSIGNMENT OF ERRORS

(Statement of Points on Appeal)

In connection with his appeal the libelant above named hereby assigns the following errors in the decree of this court entered herein.

(1)

The court erred in decreeing that libelant have and recover nothing from the respondent or the impleaded respondent.

(2)

The court erred in decreeing that the libel be dismissed.

(3)

The court erred in failing to decree that libelant have and recover costs from the respondent.

(4)

The court erred in excluding evidence of the construction given the shipping articles by the parties at the time of signing.

(5)

The court erred in excluding evidence of contemporaneous oral contract between the parties for payment of war bonus for period of internment on land.

(6)

The court erred in excluding evidence of deviation of voyage.

(7)

The court erred in denying the motion of libelant to set aside the submission and reopen the cause for introduction of further proof.

(8)

The court erred in finding that the riders attached to the shipping articles were ambiguous, vague, or uncertain.

(9)

The court erred in finding that libelant's intestate, Jack George Currie, was not entitled to war bonus for the period of internment on land west of the 180th meridian.

(10)

The court erred in failing to find and decree that libelant's intestate, Jack George Currie, was entitled to war bonus, at the rate specified in the shipping articles, for the period of internment on land west of the 180th meridian, together with interest thereon.

(11)

The court erred in finding that libelant's intestate, Jack George Currie, was not entitled to maintenance after January 1, 1942.

(12)

The court erred in failing to find and decree that libelant's intestate, Jack George Currie, was entitled to maintenance after January 1, 1942, and to payment therefor and interest thereon.

Dated, San Francisco, June 21, 1949.

Albert Michelson,  
Proctor for said Libelant.



Original filed June 21, 1949,  
Clerk, U. S. Dist. Court, San Francisco.

In the United States District Court for the Northern  
District of California, Southern Division

In Admiralty  
No. 24,807-H-G

James Keith Currie, as Administrator  
of the Estate of Jack George Currie,  
Deceased,

Libelant,

vs.

Matson Navigation Company (a cor-  
poration),

Respondent,

United States of America,

Impleaded Respondent.

## NOTICE OF APPEAL TO UNITED STATES COURT OF APPEALS

Notice is hereby given that the libelant above named hereby appeals to the United States Court of Appeals for the Ninth Circuit from the final decree entered in the above entitled cause on March 24, 1949.

Dated, San Francisco, June 21, 1949.

Albert Michelson,  
Proctor for said Libelant.

Original filed June 21, 1949,

Clerk, U. S. Dist. Court, San Francisco.

In the United States District Court for the Northern  
District of California, Southern Division

In Admiralty

No. 24,807-H-G

James Keith Currie, as Administrator  
of the Estate of Jack George Currie,  
Deceased,

Libelant,

vs.

Matson Navigation Company (a cor-  
poration),

Respondent,

United States of America,

Impleaded Respondent.

### ORDER ALLOWING APPEAL

The petition of the libelant in the above entitled cause for the allowance of the appeal to the United States Court of Appeals for the Ninth Circuit is hereby allowed and bond fixed in the sum of \$250.

Dated, San Francisco, June 21, 1949.

Louis E. Goodman,

United States District Judge.

Copy of the above and foregoing Order Allowing Appeal is hereby acknowledged this 21st day of June, 1949.

In the United States District Court for the Northern  
District of California, Southern Division

In Admiralty  
No. 24,807-G

James Keith Currie, as Administrator  
of the Estate of Jack George Currie,  
Deceased,

Libellant,

vs.

Matson Navigation Company (a cor-  
poration),

Respondent,

United States of America,

Impleaded Respondent.

ORDER

Extending Time for Filing Apostles on Appeal and  
Cross-Appeal and Docketing Appeal and Cross-Appeal  
and

Amending Designations of Contents of Apostles  
on Appeal and Cross-Appeal

It appearing to the Court that it will be impractical to prepare the Apostles on Appeal and Cross-Appeal herein within the time designated in the respective Citations herein;

Now, on motion of Messrs. Brobeck, Phleger & Harrison, Proctors for Matson Navigation Company, Respondent, Appellee and Cross-Appellant, it is hereby

Ordered that the time within which the Apostles on Appeal and Cross-Appeal shall be filed and the Appeal and Cross-Appeal docketed, be and it is hereby extended to and including September 14, 1949, and it is

Further ordered that the respective Designations of the Contents of the Apostles on Appeal and Cross-Appeal be and each of them is hereby amended so that said Apostles shall contain this Order.

Dated, July 12, 1949.

Louis E. Goodman,  
United States District Judge.





In the United States Court of Appeals  
For the Ninth Circuit

TIMOTHY E. ARMSTRONG, et al., *Appellants,*

vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

No. 12,349

JAMES KEITH CURRIE, et al., *Appellant,*

vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

No. 12,352 **CONSOLIDATED  
CASES**

DONALD G. STEWART, et al., *Appellants,*

vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

No. 12,350

Brief for Appellee and Cross-Appellee  
United States of America

FRANK J. HENNESSY

*United States Attorney*

C. ELMER COLLETT

*Assistant United States  
Attorney*

*Proctors for Appellee*

LILLICK, GEARY, OLSON,

ADAMS & CHARLES,

JAMES L. ADAMS,

*Of Counsel.*

FILED

DEC 21 1949

PAUL P. O'BRIEN,



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Nos. 12,349, 12,352, 12,350

# In the United States Court of Appeals

## For the Ninth Circuit

TIMOTHY E. ARMSTRONG, et al., *Appellants,*

vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

**No. 12,349**

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

JAMES KEITH CURRIE, et al., *Appellant,*

vs.

MATSON NAVIGATION COMPANY, a corporation,  
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**No. 12,352 CONSOLIDATED  
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UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

DONALD G. STEWART, et al., *Appellants,*

vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

**No. 12,350**

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

## Brief for Appellee and Cross-Appellee United States of America

### FOREWORD

Appellee and cross-appellee, United States of America,\*  
accepts the statement of appellants' foreword except in

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\*At the time in question the *S.S. Malama*, owned and operated  
by Matson Navigation Company, was under time charter to the



its reference to *The President Harrison* (C.C.A. 9th) 177 F.2d 107, 111. Appellants state the present cases parallel *The President Harrison*, thus suggesting this Court's decisions in such case are decisive of this litigation. For reasons hereinafter stated in this brief, appellee emphatically contends that *The President Harrison* is not dispositive of the present suits.

### STATEMENT OF JURISDICTION

Appellee does not oppose the statement of jurisdiction contained in the individual briefs of appellants.

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United States of America. When the instant libels were filed, Matson impleaded the United States of America claiming that by the terms of the charter the latter agreed to indemnify Matson if Matson were liable for the claims of libelants for war bonus and maintenance during internment. In its answers to the impleading petitions (A. 27, 53-54), the United States of America admitted such responsibility to Matson if the latter were held liable for the war bonus claims but denied such responsibility to Matson respecting any liability the latter might have for the maintenance claims. Accordingly, in the District Court the United States of America undertook the defense of the claims for war bonus during internment while Matson presented its own defense respecting the claims for maintenance during internment. When the District Court found that neither Matson nor the United States of America were liable either for war bonus or maintenance during internment it dismissed the petitions impleading the United States of America. Matson has filed a cross-appeal to preserve its claims under the impleading petitions (A. 117, 126). In the event this Court reaches a different result than the District Court regarding liability of Matson for war bonus or maintenance during internment, the issues raised by the impleading petitions and the answers thereto of the United States of America must be remanded to the District Court for determination. The United States of America continues its defense against the claims for war bonus during internment, and this brief in its behalf is directed solely to such subject. To avoid confusion as to the status of the parties the appellee and cross-appellant Matson Navigation Company will be referred to herein simply as "Matson" and the United States of America as "appellee."

## STATEMENT OF THE CASE

The basic facts are undisputed.\* Appellants were licensed and unlicensed crew members of the *S.S. Malama*, which was under time charter from Matson to appellee when she sailed from San Francisco (A. 7-8, 9, 10, 28, 53). Appellants were all members of various maritime unions (including the National Organization of Masters, Mates and Pilots of America; Marine Engineers' Beneficial Association; American Communications Association, Marine Division; Sailors' Union of the Pacific; Pacific Coast Marine Fireman, Oilers, Watertenders and Wipers Association; Marine Cooks and Stewards Association of the Pacific Coast), which had negotiated various collective agreements governing basic wages, emergency wages, and war bonus with the Pacific American Shipowners Association, an employer organization representing Matson (A. 10, 19, 20, 89-92).

The *Malama* sailed on November 25, 1941, for a voyage to "Ports in the Philippine Islands by a route, including stops, as ordered by an agency or department of the United States government \* \* \*" (A. 9, 87-88, Ex. No. 2). It arrived at Honolulu, December 8, 1941—the day after the Japanese bombed Pearl Harbor and invaded the Philippines (A. 16).† Several days later the *Malama* sailed from Honolulu on a route ordered by military and naval authorities of the United States (A. 16,† 88). On January 1, 1942 while

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\*Unless otherwise stated, all record references are to Apostles on Appeal in *Armstrong, et al. v. Matson Navigation Co.*, No. 12,349.

†Reference is to Apostles on Appeal in *Sterling, et al. v. Matson Navigation Co.*, No. 12,351. For reasons not known to counsel of the Appellee, the Reporters Transcript is contained in the Apostles in this case. The files of the clerk contain a stipulation that the determination of the issues of this case will abide the determination of the Court in the cases before it.

heading in the direction of New Zealand, the *Malama* was attacked and subsequently sunk by Japanese forces (A. 13). The crew were taken aboard the Japanese raider and held captive (A. 13). January 6, 1942, they crossed the 180th meridian, Westbound, en route to Japan where they were interned until about September 5, 1945 (A. 13-14). They were subsequently repatriated to Pacific Coast ports, recrossing the 180th meridian Eastbound on various dates (A. 14-15).

According to its obligation contained in riders attached to the shipping articles and certain of the aforementioned collective agreements referred to in the riders, Matson paid appellants all basic wages and emergency wages due and owing them for the period during which they were held captive and until arrival at Continental United States ports (A. 4, 15, Ex. No. H). Matson also paid all war bonus due appellants for the time while they were on the Japanese raider West of the 180th meridian, and after liberation, while they were on aircraft or vessels West of the same meridian during repatriation (A. 8, 16, 24, 94-95, Ex. No. I).<sup>\*</sup> Additional claims were made by appellants for war bonus and maintenance during the time they were interned by the Japanese on land. Matson refused to pay these claims and the same are the subject of this litigation.

Concededly, appellants' rights to war bonus are contractual ones dependent upon the contract of hire opera-

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<sup>\*</sup>In each brief submitted for appellants there is a misleading statement of what amount of war bonus was paid appellants. It is stated that they were paid no war bonus while West of the 180th meridian. This is only true insofar as it applies to the time while they were interned on land. Otherwise, as stated above, they were paid a war bonus while aboard vessels West of the 180th meridian.

tive at the time they "signed on" the *Malama* (A. 2-3). The pertinent portions of this contract are contained in riders attached to the shipping articles and in collective supplementary bonus agreements (A. 92). The provisions of the rider dealing with the payment of benefits to licensed personnel, including the radio officer, while aboard the *Malama* and with the eventuality of internment or destruction of that vessel, read as follows:

"The Matson Navigation Company agrees to pay war risk bonuses to the crew of the SS *Malama* from the crossing of the 180th Meridian Westbound until recrossing the same Meridian Eastbound as follows:

Licensed Deck Officers:  $66\frac{2}{3}\%$  of the basic monthly wages effective as of Oct. 1, 1941;

Licensed Engine Officers:  $66\frac{2}{3}\%$  of the basic monthly wages effective as of Oct. 1, 1941;

Radio Officer:  $66\frac{2}{3}\%$  of the basic monthly wage effective as of Oct. 1, 1941.

"In the event the vessel is ordered by an Agency or Department of the United States Government to return via another trade route, war risk bonuses will be paid while the vessel is in any of the war zone Areas I to VI inclusive at the rates described in the supplementary agreements between the various Marine Unions and the Pacific American Shipowners Association at San Francisco.

\* \* \* \* \*

"*In the event the vessel be interned, destroyed or abandoned as a result of war operations and be un-*



able to continue her voyage, basic wages and emergency wages specified in the collective bargaining agreements between the parties shall be paid to the date members of the crew arrive in Continental United States ports and the employes shall be repatriated to a Continental United States port. *While the employes are in the war zone areas described in the supplementary agreements covering war risk bonuses payable to Licensed Officers, war risk bonuses shall also be paid to them at the rate of 66 $\frac{2}{3}$ % of the said basic wages in Areas I to V inclusive, and 25% in Area VI.*" (Italics added.) (Ex. No. 2.)

The rider governing the unlicensed personnel is substantially the same, and its material provisions read as follows:

"The Matson Navigation Company agrees to pay war risk bonuses to the crew of the SS Malama from the crossing of the 180th Meridian Westbound until recrossing the same Meridian Eastbound, as follows:

Unlicensed

Deck Personnel: \$80.00 per month;

Unlicensed

Engine Personnel: \$80.00 per month;

Steward's Personnel: \$80.00 per month to all employes entitled to receive \$120.00 or less as basic monthly wages as of Oct. 1, 1941; 66 $\frac{2}{3}$ % of the basic monthly wages as of Oct. 1, 1941 to all employes entitled to receive basic monthly wages in excess of \$120.00.



“In the event the vessel is ordered by an Agency or Department of the United States Government to return via another trade route, war risk bonuses will be paid while the vessel is in any of the war zone Areas I to VI inclusive at the rates described in the supplementary agreements between the various Marine Unions and the Pacific American Shipowners Association at San Francisco.

\* \* \* \* \*

*“In the event the vessel be interned, destroyed or abandoned as a result of war operations and is unable to continue her voyage, basic wages and emergency wages specified in the collective bargaining agreements between the parties shall be paid to the date the members of the crew arrive in a Continental United States Port, and the employes shall be repatriated to a Continental United States Port. War risk bonuses at the rates specified in sub-division (b) paragraph 1 of the supplementary agreements between the parties shall be paid while employes are in the war zone areas defined therein.”* (Italics added.) (Ex. No. 2.)

At this point it is advisable to call special attention to certain features of the two riders quoted above. Before doing so it should be made clear that the primary object of both the riders and the supplementary bonus agreements, which will be discussed hereinafter, was to prescribe extra compensation to crew members in the form of war bonus on account of war hazards to which they might be exposed by virtue of the vessel on which they were employed making a voyage into certain danger zones. This primary object may be stated more simply as a pro-

vision for sailing bonuses to crew members on voyages made hazardous by war conditions. The matter of internment or destruction of the vessel aboard which the crew members were employed at this time, before the United States was engaged in the war, was a remote possibility and provision for such an eventuality was only an incident to the main purpose of prescribing sailing bonuses which was foremost in the minds of the parties.

An examination of the riders will disclose the following features: First, provision was made for the amount of bonus to be paid to the crew members in respect to the known voyage on which the vessel was about to sail. As is pointed out elsewhere in this brief, the articles called for a trans-Pacific voyage to the Philippine Islands with certain other routing liberties. Inasmuch as only a portion of such a voyage was considered hazardous by virtue of war conditions, it was specified that war bonus became payable on the voyage only when the vessel crossed the 180th meridian Westbound and discontinued when the vessel recrossed the same meridian Eastbound. This feature of the riders dealt with the sailing bonus for the anticipated trans-Pacific voyage and was geared to the wages received by the various crew members according to their ratings. The meridian limitations and rates prescribed coincided with and reasserted those set forth in the supplementary agreements for this particular war zone or voyage.

The second feature of the riders that should be particularly noted is the provision for the payment of war bonus if the vessel were diverted from her original voyage and were ordered to a different route. Since what rerout-

ing of the vessels might be ordered by the United States Government could not be anticipated at the time the articles were opened, it was provided that while the vessel was in a war zone or on a voyage defined in the supplementary agreements war bonus should be paid at the rates specified in such agreements. These agreements, of course, defined all the war zones or voyages in respect to which bonuses might be payable. By virtue of the second paragraph of each rider the applicable war bonus prescribed in the supplementary agreements for any particular war zone or voyage became automatically operative when the vessel entered upon such war zone voyage.

The third feature of the riders is the one with which we are most directly concerned in this litigation. This deals with the provision contained in each rider in the event of internment, destruction or abandonment of the vessel as the result of war operations. Upon the happening of such an event it was provided that basic wages and emergency wages as specified in the basic collective bargaining agreements between the parties should be paid to the date the crew members arrived in a Continental United States Port. Furthermore, the requirement was imposed on Matson, as the employer of the crew members, to repatriate them to a Continental United States Port. In addition, and most significantly to the issues involved in this litigation, provision was made for the payment of war bonus to the crew members while aboard such a repatriating vessel. Again, because it was impossible to determine what war zone voyages the repatriating vessel or vessels would enter upon in returning the crew members to a Continental United States Port, it was necessary to make ex-

press reference to the supplementary agreements, in the same manner and for the same purposes that such reference was made in the case of the vessel being rerouted by the United States Government. Accordingly, it was specified that war bonus would be payable to the crew members while in the war zone areas or on war zone voyages as defined in the supplementary agreements.

It should be particularly noted in connection with the consideration of the two riders, that in the event of the internment, destruction or abandonment of the vessel, as occurred in the present case, reference to the supplementary bonus agreements was *expressly and specifically* made in order to determine when war bonus would be payable.\* The unlicensed personnel rider also required reference to these agreements in order to determine the rate of bonus which depended upon the amount of the basic monthly wage and which varied according to the war zone voyages on which the vessel was engaged. The licensed personnel rider incorporated the applicable percentage rates contained in the supplementary agreements governing such crew members because their rates were not dependent upon a minimum basic monthly wage.

The pertinent portions of these supplementary agreements, to which express reference was made in the riders, are substantially the same. For the sake of brevity here, a typical licensed personnel agreement is set forth in the Appendix and the material provisions of only one of the

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\*Appellants have studiously avoided reference to this provision of the riders in their argument and have thus completely misconceived the issues of this litigation.



unlicensed personnel agreements (Ex. No. 6)\* is now quoted:

“I. The following war bonus rules shall govern the parties hereto—

“a) There shall be five war risk zones; namely:

\* \* \* \* \*

“III. Trans-Pacific *voyages* to Japan, Philippine Islands, China, Indo-China, East Indies, Malayan Peninsula. (After crossing the 180th Meridian westbound, until recrossing the same Meridian eastbound.) (Italics added.)

\* \* \* \* \*

“4. War Risk Insurance in the sum of \$5,000 shall be furnished to members of the crews of vessels on voyages provided for in this agreement.

*“In the event a vessel is interned, destroyed or abandoned as a result of war operations and is unable to continue her voyage, basic wages and emergency wages specified in the collective bargaining agreement between the parties shall be paid to the date the members of the crew arrive in a Continental United States port and the employees shall be repatriated to a Continental United States port. War bonuses at the rates specified in subdivision (b) of paragraph 1 hereof shall be paid while employees are in the war zones defined herein. (Italics added.)*

\* \* \* \* \*

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\*The supplementary bonus agreement quoted is that governing crew members in the unlicensed deck department represented by the Sailors' Union of the Pacific. Similar agreements governing the unlicensed engine room department represented by the Pacific Coast Marine Fireman, Oilers, Wipers and Watertenders Association (Ex. No. 7) and cooks and stewards represented by the Pacific Coast Marine Cooks and Stewards Union (Ex. No. 8) contain identical provisions to those quoted above.



“6. The provisions of this agreement shall be effective on all voyages shipping articles for which were entered on or after August 16, 1941 or upon any voyage to which the provisions herein are made applicable by special agreement or rider attached to shipping articles.”

The District Court construed the riders attached to the articles, as it was required to, with the applicable supplementary agreements, and held that the contract of hire did not contemplate the payment of war bonus during internment on land (A. 92-94, Findings of Fact XI, XIV). The maintenance claims were also denied.\*

### THE ISSUES

The principal issue is whether the riders attached to the *Malama* shipping articles, construed with the applicable supplementary agreements, provided for the payment of a war bonus during internment on land by the enemy. Subsidiary issues, and largely irrelevant, arise from the trial court's exclusion of evidence advanced by appellants to alter the plain language of the contract of hire, and to establish a deviation. Finally, appellants still press claims for maintenance allowances during the internment period.

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\*Contrary to the assignments of errors and the allegations in the brief in No. 12,350, the District Court did not allow costs to Matson or Appellee. An earlier allowance of costs was struck from the final decree of the District Court (A. 101).

**ARGUMENT****I. The Shipping Articles, the Riders Attached Thereto, and the Supplementary Agreements Referred to Therein Were Plain, Certain, and Unambiguous and Clearly Did Not Entitle Appellants to War Bonus During Internment on Land.**

Because of appellants' contention that *The President Harrison* is dispositive of this case, which appellee emphatically denies, frequent reference to that case is necessary. Therefore, at the outset counsel for appellee wish to assert, so as to avoid subsequent confusion, that there is no intent on their part to reargue *The President Harrison*. Reference to it is made only to demonstrate its non-applicability to this litigation. It is not necessary here, as it was in *The President Harrison* case, to consider the relationship between operative collective bargaining agreements and individual contracts of hire in the form of shipping articles and attached riders. In *The President Harrison* case consideration of the collective agreements along with the shipping articles and attached riders was urged because the same were operative by their own express terms in respect to the parties and the subject matter in dispute, because they circumscribed the rights of the parties to vary collective terms of employment by individual contracts of hire, because they and the shipping articles and attached riders together prescribed the terms of employment and were construable together under controlling rules of construction, and because the riders were ambiguous and the collective agreements furnished the required clarification.

For reasons which presently will be stated, consideration of the supplementary bonus agreements in the pres-

ent case is in no respect dependent upon acceptance of the foregoing propositions. For the purposes of the present case appellee will adopt the contention of the appellants here and the views expressed by this Court in *The President Harrison* case that the shipping articles are the controlling contract of employment. Appellee points out in this connection, however, that the riders attached to the shipping articles, by express terms of reference, *require* consideration of the supplementary bonus agreements. Appellants, in their briefs, studiously refuse to acknowledge this evident and significant fact.

Appellee agrees with appellants that the entire contract of hire was clear and unambiguous.\* Nevertheless, disagreement exists over the contents and construction of this contract. Appellee submits that the only rational interpretation of the contract of employment bars the claim to a war bonus during internment on land. The District Court so held after the fullest consideration, and its findings are entitled to great weight.

See, *e. g.*,

*Rideout v. Charles Nelson Co.* (C.C.A. 9th) 55 F.2d 783, 786;

*The Heranger* (C.C.A. 9th) 101 F.2d 953, 957.

Appellee agrees with the appellants that the portions of the shipping articles relevant to this litigation are con-

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\*Contrary to the assignment of errors of appellants, the District Court did not find that the riders attached to the shipping articles were ambiguous. Findings of fact of the District Court resting on the contract of hire standing alone, adequately support its decision. (Findings of Fact XI, XIV.) Also contrary to a suggestion contained in appellants' brief submitted in No. 12,350, counsel for appellee did not assert that the riders attached to the shipping articles were ambiguous. Counsel for appellee expressly denied that they were ambiguous. (A, No. 12,351, p. 33.)

tained in riders attached to the shipping articles. The pertinent portions of both riders have already been quoted in the statement of facts. It could not be clearer that both of them require reference to the collective supplementary bonus agreements for determining *when* the war risk bonus is to be paid in the event the vessel is interned, destroyed, etc. The licensed personnel rider states that the war risk bonuses are to be paid "while the employees are in the war zone areas described in the supplementary agreements \* \* \*." That governing unlicensed personnel states that the war bonus is to be paid "at the rates specified in subdivision (b), paragraph 1 of the supplementary agreements between the parties \* \* \* while employees are in the war zone areas defined therein." Thus, these supplementary agreements, which had been negotiated by union representatives representing the appellants and the P.A.S.A., representing Matson, are expressly made an integral part of the contract of employment by the riders attached to the shipping articles. By express requirement of the riders, one must look to these agreements for the description of the war zone area, which delineates when bonus should be paid. Failure of appellants to take cognizance of this requirement of the riders and to consider these agreements results in a complete misconception of the contract of hire which governs their rights. As a result they blindly place reliance on this Court's decisions in *The President Harrison*.

*The President Harrison*, however, is not dispositive of this litigation. Appellants assert that the articles in *The President Harrison* and those herein involved are substantially the same. Close examination of the riders at-



tached to the two shipping articles reveals a material difference. In *The President Harrison* the riders did not expressly, as in this case, refer to the supplementary bonus agreements. In *The President Harrison* counsel for appellee contended, and the District Court found, that a proper interpretation of the shipping articles required consideration of the supplementary bonus agreements, because, among other things, the riders attached to the articles were uncertain and merely inartful attempts to paraphrase the supplementary agreements.\* However, this Court did not agree with this conclusion in *The President Harrison*. It expressly held that the rider standing alone contained a definition of the war zone area; two paragraphs of the *rider* were construed together to establish this. See 177 F.2d at 109. Thus, the theory adopted by this Court in *The President Harrison* obviated reference to the supplementary agreements. However, the express language of the riders attached to the *Malama* articles *does* require reference to the supplementary bonus agreements. Therefore, contrary to appellants' contentions, the construction of *The President Harrison* shipping articles is not authority for those involved in the present case.

Thus, we reach the major issue of this litigation, to wit, to what extent is a right to war bonus during internment on land created by the supplementary agreements to

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\*Counsel for appellee never stated that the issues in *The President Harrison* and in this case were the same, as counsel for appellants in the brief submitted in No. 12,350 would suggest. Instead, counsel for appellee stated that he could point out the significant differences between the riders involved in each case in "ten minutes," which would have been an indication of the distinction made above. (A. No. 12,351, 97-102.) A fair reading of the colloquy clearly shows that counsel did not concede that *The President Harrison* was dispositive of this case.



which the riders attached to the *Malama* articles refer. Six supplementary agreements, of which the pertinent portions are substantially alike, govern appellants' rights and Matson's obligations. The interpretation of these collective agreements is certainly now squarely and directly placed before this Court, perhaps, for the first time.

Counsel for appellee must concede that until this Court filed its amended decisions in *The President Harrison* case on September 9, 1949, they considered that this Court's interpretation of these same agreements in *Steeves v. American Mail Lines, Ltd.* (C.C.A. 9th) 154 F.2d 24, 25, was necessary and vital to the ultimate determination and was not *dictum*. This belief was also held by the District Court in the present case and in *The President Harrison*. Furthermore, counsel for the appellants in this case, who were also counsel for the appellants in *The President Harrison*, never once asserted a contrary view. In reference to two of these identical collective agreements governing unlicensed personnel this Court stated in the *Steeves* case:

“Since, if rational, we must construe the second paragraph [of the rider] to give effect to its agreements, we construe the provision of the union agreement for period of bonus during the return voyage of the ship to the 180th meridian as not ‘applicable’ to the specific agreement to pay one during the period of captivity after the ship's destruction in Manila.

“The same is true of the cooks and stewards union agreement. There, the war bonus period is during the ship's voyage westerly from and easterly to the 180th meridian. It is not applicable to a case of the destruction of the vessel and the subsequent period

of captivity and repatriation specifically provided for in the second paragraph of the rider.

“It was thought that there was some ambiguity in the provisions of these instruments which warranted testimony as to their meaning. We do not agree. It requires no testimony to make it clear that the union agreements did not provide for the bonus during the period specifically provided in the shipping articles.”  
154 F.2d at 25.

Since this interpretation of these collective agreements has been characterized by this Court in *The President Harrison* as *dictum*, then it is equally certain by the same standards that any interpretations of these same agreements rendered by this Court in the latter case are no more conclusive for the following reasons:

*First:* The disposition of the bonus claims of the licensed personnel indicates that the shipping articles standing alone were considered the measure of appellants' rights. The rate for computing the war bonus contained in the supplementary agreements was higher than that in the rider, but the Court held that the lower rate of the rider was controlling. See *Griffin v. American President Lines, Ltd.* (C.C.A. 9th) 177 F.2d 111, 113. This clearly establishes that consideration of the supplementary agreements was not necessary to the holding of the case, since when a variance as to a vital term existed between them and the articles, the latter controlled. Therefore, any statements concerning the agreements are merely *dictum*, on the authority of the Court's disposition in *The President Harrison* of its former language in the *Steeves* Case.

*Second:* The Court's discussion of the supplementary agreements appears to be support merely for its interpretation of the shipping articles. There was no independent consideration of the agreements standing alone, which is indicated by the Court's statement that the agreements were "construed in connection with \* \* \* the rider." See 177 F.2d at 109. Those riders, however, were in no way relevant to or supportive of the meaning of the agreements. Counsel admit that they argued in *The President Harrison* that the supplementary agreements were relevant to and supportive of the meaning of the riders. This was so because, according to counsel's contention, the riders were drawn to conform with the agreements. Counsel emphatically contend, however, that the rider was not relevant to or supportive of the meaning of the supplementary agreements. The reason is clear. The agreements were drafted to cover all shipping operations of all member companies of the P.A.S.A. *The President Harrison* articles and riders, at most, could only govern the rights of its crew members; its articles and riders in no way could qualify rights under the collective bonus agreements of seamen sailing aboard other vessels under different articles and for other employers. A construction of the supplementary agreements made dependent upon *The President Harrison* articles and riders would create such a qualification. Therefore, to suppose that *The President Harrison* contains an interpretation of these supplementary agreements standing alone would be to create a novel rule of construction indeed.

For the reasons stated above, we repeat our earlier assertion that the interpretation of these supplementary bonus agreements is now squarely and directly presented to this Court for initial determination. Even to this day counsel for the appellants have not contended that these agreements, specifically referred to in the *Malama* riders, create a right to war bonus during internment on land. We challenge them now to recognize the existence of these collective bargaining agreements, to which express reference is made in the riders, and to join issue on this single, major point of whether these agreements define war zones in such terms as to provide for war bonus while interned on land.

We unhesitatingly and confidently direct attention to our analysis of the pertinent portions of the supplementary agreements. The riders require that we examine the description of the war zone areas in the agreements, since a war bonus is to be paid "while the employees are in the war zone areas described" therein. The language in the three supplementary agreements governing unlicensed personnel is identical and reads as follows:\*

"a) There shall be five war risk zones; namely:

\* \* \* \* \*

"III Trans-Pacific *voyages* to Japan, Philippine Islands, China, Indo-China, East Indies, Malayan Peninsula. (After crossing the 180th Meridian Westbound, until recrossing the same Meridian Eastbound.)" (Italics added.)

Construing the pertinent portions of the riders attached to the articles with those of the supplementary agree-

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\*The corresponding provisions in the licensed personnel agreements are set forth in the Appendix.



ments, as we are required to, we have the following provision:

“In the event *the vessel be interned, destroyed or abandoned as the result of war operations* and is unable to continue her voyage, *basic wages and emergency wages* specified in the collective bargaining agreements between the parties *shall be paid to the date members of the crew arrive in Continental United States ports*, and the employees shall *be repatriated to a Continental United States port. War risk bonuses \* \* \** shall be paid while employees are in the war zone areas defined \* \* \*” as “*Trans-Pacific voyages to (the) \* \* \* Philippine Islands \* \* \**. (After crossing the 180th Meridian Westbound, until recrossing the 180th Meridian Eastbound.)” (Italics added.)

It could not be clearer that the war bonus is compensation for the risks incurred by employment on a vessel voyaging in specified areas. By no rational interpretation of the word “voyage,” which is the term chosen to delineate the war zone area, can internment on land be comprehended within its meaning.

This intent to make the right to war bonus dependent on the risks incurred from employment on a vessel is even more evident in other provisions of the supplementary bonus agreements to which the riders expressly refer. We have previously been considering the rights of crew members in the event of internment or destruction of the vessel. These provisions of the bonus agreements, however, were merely incidental to the major purpose of these agreements. At the time these agreements were negotiated, several months before the startling and sur-



prising attack by the Japanese on Pearl Harbor, the possibility of internment or destruction of an American vessel was remote and the possibility of internment of the crew so improbable as not even to warrant mention or specific provision for such an event. On the other hand the increased physical hazards to crew members aboard vessels operating in war zones formed the basis for added compensation or bonus to them for exposure to such risks. Consequently, the major subjects for negotiation were a determination of the areas or voyages in respect to which these added war hazards existed and of the amount of the increased compensation or bonus warranted for sailing on such voyages.

Therefore, the supplementary agreements with the S.U.P., M.F.O.W.W., and M.C.& S. (Ex. Nos. 6, 7, 8) at the outset, quite naturally, relate the payment of war bonuses to the period when crew members are aboard vessels in war zones. The preamble clause which defines the purposes of the contracts, in the M.F.O.W.W. agreement reads as follows:

“Whereas, the parties hereto are engaged in the negotiation of a collective bargaining contract relative to wages, hours, and working conditions for members of the Union and desire to provide a collateral or supplementary agreement for bonuses payable to members of the Union *on vessels going into war zones;*”\* (Italics added.)

Language could not more clearly provide that war bonuses were payable only while the seamen were on vessels. The

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\*The preambles of the S.U.P. and M.C.&S. agreements differ in language, but contain substantially the same content in this respect.

subsequent definition of the "war zone" as a "voyage" and the provision allowing a war bonus only while in the war zone are the logical development of this primary purpose.

When it is properly understood that the major purpose of these agreements was to provide for bonus while the crew were aboard vessels on voyages in war zones and that providing for the consequences of internment of the vessel was incidental, all the provisions of the riders, which incorporate these agreements, are consistent and meaningful. For example, the opening clause of the riders provides that a war bonus was due the crew from the crossing of the 180th meridian Westbound until recrossing the same meridian Eastbound. No reference to the bonus agreements is made. The reason is clear. At the time of signing on, it was known that the voyage was a trans-Pacific one. The opening clause is a paraphrase of the definition of the war zone as "Trans-Pacific voyages" (limited to that portion West of the 180th meridian) contained in the bonus agreements, so that reference to the agreements was unnecessary. However, in the event of interruption of the contemplated voyage, either by governmental alteration of the voyage or by internment or destruction of the vessel, a paraphrase of bonus rights contained in the agreements was not possible since it was unknown what war zone voyage might then be undertaken. Consequently, express reference in both instances incorporated the bonus agreements, which by their language make clear that a war bonus was payable only while on board a vessel engaged on a voyage in one of the specified areas.

Any other interpretation would render the supple-

mentary agreements meaningless. This may be demonstrated by a consideration of what the bonus rights of appellants would have been had they signed on for a voyage to a different war zone. All of the war zone areas are defined as "voyages." For example, War Risk Zone II is defined in the following manner:

"Trans-Atlantic voyages to Russia (Archangel, etc.)  
(Whole voyage)."

It should be noted that war bonus on such a voyage is payable during the entire voyage and not after the vessel crosses a particular meridian, as in the case of trans-Pacific voyages. If the vessel were destroyed on such a trans-Atlantic voyage and the crew were interned in Germany surely this place of internment would not be deemed included in the war zone definition of "Trans-Atlantic voyages to Russia." This inescapable conclusion demonstrates that the definitions of war zones in terms of voyages precludes application of war bonus to a period of time or to a geographical area of land. A war zone defined as a trans-Pacific voyage but limited to the dangerous portion lying West of the 180th meridian is no less a definition in terms of a voyage than a war zone defined as a trans-Atlantic voyage (whole voyage). Hence, crew members interned on land are not in a war zone, as defined in the supplementary agreements, no matter where that land is geographically located.

Since these war zone areas are defined in the bonus agreements as "voyages," there is no rational basis for treating the same word used in an agreement as having a different meaning when used similarly in the same

agreement. To do so would violate an elementary rule of construction, *i.e.*, a written document should be interpreted as a whole so as to make all parts consistent. See *Cal. Civ. Code*, §§ 1641, 1642; *Cities Service Gas Co. v. Kelly-Dempsey & Co.* (C.C.A. 10th) 111 F.2d 247, 249.

The provisions in the supplementary agreements for port bonuses in certain cases further documents the intent to relate war bonuses to the position of the vessel. For instance, in addition to the port bonus of \$100 paid for calling at Suez, or any other port subject to regular bombings, an extra \$5.00 is provided "for each day beyond five days that the *vessel* is in that port." (Ex. Nos. 6, 7, 8). Thus, port bonuses are geared to vessels in the same manner that bonuses on voyages depend upon a vessel engaging in such a voyage. Finally, in the M.M. & P., M.E.B.A., and A.C.A. supplementary bonus agreements machinery provided for the adjustment of war bonus rates, dependent on future events, which was geared to "war risk insurance rates paid on hulls of American flag *vessels* operating in all areas above described." Clearly, if war bonuses were dependent upon war risks in all areas, including land, war risk insurance rates on vessels would be an inappropriate measure of such risks, since these rates are determined only by the navigational war risks to which vessels are subjected. The adoption of this standard for future modification of war bonus rates is additional clear indication that war bonuses were payable only in relation to a vessel operating on a voyage described as a war risk area.

In concluding argument of this point, appellee submits that the language of the supplementary agreements, made



an integral part of the riders by reference, clearly establishes that a war bonus was due only while the men were in a war zone area which is defined as being when a vessel is on a voyage in specified areas. Although Admiralty Courts traditionally have been solicitous of the welfare of seamen, appellee contends that this case would be an improper one for indulging in any presumption that grants appellants benefits not intended by the governing contract. Appellee emphatically asserts that there is no ambiguity in the contract of hire, and that its clear meaning precludes payment of war bonus during internment on land. Should the Court disagree with appellee and conclude for reasons not apparent to appellee that the contract is ambiguous, the Court should not adopt presumptions which would distort the meaning of the contract made manifest by application of paramount rules of construction. It should also be borne in mind, if there is any ambiguity to be found in this contract of hire, that such ambiguity is in a collective bargaining agreement. This is not the type of agreement that seamen enter into as individuals with supposedly unequal powers of understanding. Nor is it an agreement that the employer alone drafted so as to have doubts, not otherwise removable, resolved against him. As Judge Goodman ably pointed out in his opinion in *The President Harrison*, 73 F. Supp. 944, 948, the seamen represented by the maritime unions negotiating these contracts can no longer be considered defenseless and incapable of looking after their own interests. Their rights are vigilantly and militantly protected by such unions, as counsel for appellants must concede.



Finally, the Court should not indulge any presumption so as to write an entirely new contract which would place appellants in a more advantageous position than that held by many thousand persons similarly situated. The scheme of compensation contained in these supplementary agreements and the riders attached to the shipping articles, as contended for by appellee, is identical to that adopted by the entire shipping industry.

See:

Maritime War Emergency Board, Decision No. 5,  
Rev.\* (Ex. K).

See also:

*Mason v. Texas Co.* (C.C.A. 1st) 171 F.2d 559, 562,  
*cert. den.*, 93 L.Ed. 1035;

*Montoya v. Tidewater-Associated Oil Co.* (C.C.A.  
2d) 174 F.2d 607, 610, *cert. den.*, 94 L.Ed. 58.

It is as generous a compensation scheme as that adopted by Congress to compensate United States employees taken captive by the enemy (see *56 Stat. 143*, 50 U.S.C. App. §§ 1001-1018), or the employees of contractors with the

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\*Counsel for appellee does not press the contention herein, as they did in *The President Harrison*, that the decisions of the Maritime War Emergency Board govern the seamen's rights to war bonuses. Failure to make that contention is not to be considered a concession by appellee that those decisions do not so control. Appellee is merely respecting this Court's prior determination of this issue. However, in view of the fact that a petition for certiorari is to be filed in the Supreme Court of the United States in *The President Harrison* cases, this issue may be considered by that Court and become critical to the ultimate disposition of that case. Should the Supreme Court of the United States disagree with this Court's previous conclusion on this issue, appellee reserves the right to argue that appellants' rights herein should be governed by the decisions of the Maritime War Emergency Board.

United States taken captive by the enemy (see 56 Stat. 1028, 42 U.S.C. §§ 1701-1717). These references indicate that Matson and appellee have not attempted to discriminate against appellants, but, on the contrary, that P.A.S.A. and Matson actually anticipated the entire shipping industry and Congress in providing a full measure of compensation for employees subjected to war risks. Having granted and respected these rights, Matson is now entitled to have honored its rights under the contract.

**II. The District Court Did Not Err in Excluding Evidence Purporting to Establish That the Parties Gave a Contrary Meaning to the Contract of Hire by Their Actions.**

Appellants contend that the District Court erred in failing to admit certain evidence, and refusing to reopen after submission for admission of other evidence, which purportedly establishes an interpretation given the contract of employment by conduct of the parties. Appellee submits that this evidence was properly excluded by the trial court. Concededly, appellants by their pleadings pegged their rights on the written contract contained in the shipping articles of the *Malama*, which expressly require consideration of the supplementary agreements. Appellants contend, and appellee agrees, that the contract of hire is clear and unambiguous. This should clearly prevent the alteration of a written contract by vague testimony elicited from interested parties six years after the occurrence of the event in question, to wit, the signing of the shipping articles.\* All of the policy reasons supporting

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\*Counsel for appellee do not intend to retreat from the contentions they made in *The President Harrison* by this statement. In that case they contended that the contract of hire included

the precept of the Parol Evidence Rule could not be more clearly present. It has frequently been held that the contract of hire as evidenced by the shipping articles cannot be changed by parol evidence, short of showing fraud.

See:

*The Lakme* (Wash. N.D.) 93 Fed. 230, 231;

*The Ucayali* (E.D. N.Y.) 164 Fed. 897, 899;

*Foreman v. J. M. Benas & Co.* (S.D. N.Y.) 247 Fed. 133, 134 (A. Hand, J.).

However, assuming the admissability of this evidence, which has been included in the record, appellants' construction of the contract is not supported by it. Appellants contend that the deputy shipping commissioner who was present at the signing of the shipping articles, in response to inquiries of crew members, stated that a war bonus would be paid until repatriation to a United States port, if the crew were captured and interned. It is stated that this was the understanding of the master of the vessel, who consequently remained silent when this information was given. The affidavit of the master is relied upon to establish this. The allegations in the affidavit do not support this contention. It is therein recited that the question asked the deputy shipping commissioner was, "what would happen if the *vessel* was captured or interned?"

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agreements apart from the shipping articles. This contention rested on the nature of the shipping articles and the collective bargaining agreements. It is unnecessary in this case to establish the applicability of these materials since the articles expressly incorporate them. Discussion is unnecessary to show the difference between agreements expressly incorporated and testimony of the understanding held by the seamen at the time the agreements were signed.

(A. 71). The question was directed to the consequences of internment of the vessel, and not to that of the men. At this time, November 25-28, 1941, the United States was not yet at war. The suddenness of the attack on Pearl Harbor with its consequent surprise to the American public is adequate evidence, of which the Court may take judicial notice, that our entry into the Pacific war was not considered imminent. Consequently, there is no basis to assume that the parties did not expect that in the event of capture of an American vessel the crew members would be repatriated by customary international channels. Internment of the crew was not anticipated, nor should it have been. Thus, the commissioner's reply that "wages and bonus would go on until they got back to the United States" (A. 72) was an accurate interpretation of the riders insofar as they provided for war bonus during repatriation. At best the commissioner's statements are ambiguous and do not possess that quality of proof necessary to overcome the strong presumption in favor of the written contract. See *North. Mut. Life Ins. Co. v. Nelson*, 13 Otto 544, 103 S.Ct. 436, 438.

The Court of Appeals for the Second Circuit has recently rendered a decision fully supporting appellee's contentions.

*Montoya v. Tidewater-Associated Oil Co., supra.*

In that case libelant, a seaman, testified that he had a limited ability to read English, and that he was not shown the page of the shipping articles containing provisions for war bonus in conformance with decisions of the Maritime War Emergency Board. He further testified that the



shipping commissioner, in response to a question concerning the right to war bonus, stated that it continued until the seaman returned to New York. Nevertheless, the Court of Appeals held that libelant's right to war bonus was governed by the written provisions of the articles and not by the libelant's understanding of his rights derived from the commissioner's remarks. Two cases could not be more identical. Should the Court in this case approve the appellants' contentions that the excluded testimony was admissible for altering the written provisions of the contract of hire, a clear conflict between the circuits would be created.

In the *Montoya* decision the Court did suggest that the rule might be otherwise in the case of fraud. However, there is not the slightest indication of fraud in this case, nor do the appellants make such a claim. If anything, a stronger showing of fraud might have been made in the *Montoya* case than in this. There, libelant testified that he did not read English well, and that he was not shown the controlling provision of the shipping articles. In this litigation appellants' witnesses, on cross examination, stated that they knew that union agreements covered the subject of war bonuses (A. 36, 37\*); that a union representative was present at the time the articles were signed and union members relied upon him to protect their interests (A. 56, 57\*); that the commissioner read to them the governing portion of the articles in their entirety (A. 58\*); and that the riders attached to the articles were also attached to the fo'c'sle card up to the time of sinking (A. 80, 81\*).

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\*Apostles on Appeal in *Hilda Sterling v. Matson Navigation Co.*, No. 12,351.



In summary, appellee submits that the District Court did not err in excluding testimony offered for the purpose of altering the plain terms of a written contract. Appellee further contends that the excluded testimony does not support appellants' argument that the parties by their conduct construed the contract of hire in a manner supporting the interpretation urged by the appellants.

### **III. The District Court Did Not Err in Excluding Evidence Purporting to Establish a Contemporaneous Oral Contract Governing War Bonuses.**

Appellants also contend that the excluded evidence would establish a contemporaneous oral contract specifically providing for the payment of war bonus while crew members were interned on land. This farfetched contention is entirely unsupported by the evidence or law. The libelants did not plead an oral contract; their libels are specifically predicated on a written contract. No motion was made to amend. Appellants cannot now switch their theory of the case from a written to an oral contract. There is ample authority for the proposition that there can be no material variance between allegations of a libel and the evidence offered at the trial to sustain the libel.

*The I.S.E. 2* (C.C.A. 9th) 31 F.2d 107; 1929 A.M.C. 707;

*The Columbia* (N.D. Cal.) 1924 A.M.C. 592; *aff'd* 4 F.2d 673;

*The General George W. Goethals* (E.D. N.Y.) 1928 A.M.C. 378;

*The Mar Mediterraneo* (S.D. N.Y.) 1928 A.M.C. 511, 513.

Moreover, if all the stricken testimony were admitted, there is nothing to suggest that a valid oral agreement governing war bonus rights was reached. The written contract, which consists of the articles, the rider attached thereto, and supplementary agreements referred to therein, expressly governed the question of war bonuses. A collateral oral contract conflicting with the terms of a written contract specifically covering the subject matter may not be established.

See,

*Sickelco v. Union Pac. R. Co.* (C.C.A. 9th) 111 F.2d 746, 750.

#### **IV. The District Court Did Not Err in Excluding Evidence Purporting to Establish a Deviation.**

Appellants contend that evidence excluded by the trial court would have established a deviation entitling them to the fullest amount of compensation. The correctness of the trial court's ruling in excluding this evidence is even more clear, if possible, than its other exclusionary rulings. The appellants did not claim a deviation in their libels, so that allowing introduction of this evidence would improperly create a material variance between the proof and the pleadings. Moreover, it is not clear how consequent benefits to appellants are to be derived from establishing a deviation. Ordinarily deviation is urged to abrogate contracts of affreightment or policies of marine insurance. In respect to their attempt to apply this doctrine here we wonder if counsel for appellants are prepared to accept the logical consequence that the shipping articles were abrogated by the deviation. Since any claim for war

bonus which is entirely dependent on this contract would then automatically collapse, appellee will join appellants in a stipulation to this effect, if desired. At most, however, a deviation respecting shipping articles can render a ship operator liable only for wages during the deviation or damages directly caused by the deviation. Neither Matson nor appellee has ever denied that appellants were entitled to basic and emergency wages until repatriated to a United States port, and in fact Matson has paid the same to appellants. Assuming that the destination was changed from the Philippine Islands to New Zealand after December 7, 1941, this would have added security to the voyage rather than expose the crew to greater risks. If this change were a deviation, it is not shown what damage, if any, it caused appellants. The cases cited by appellants are not pertinent to this litigation; nor do they indicate how a deviation can confer a right to a special form of compensation such as war bonus not otherwise granted by contract.

Furthermore, it is patent that there was no deviation. The shipping articles describe the voyage of the *Malama* as follows:

“From the Port of San Francisco, California, to Ports in the Philippine Islands by a route, including stops, as ordered by an agency or department of the United States Government \* \* \*”

The testimony which appellants sought to introduce does not establish that the destination of the *Malama* had been altered; it merely shows that the *Malama* was heading to New Zealand at the time it was sunk. The articles clearly state that the “route, including stops” may be defined

by the order of an agency of the government. The Court may take judicial notice of the fact that at the time the *Malama* sailed from Honolulu on December 17, 1941, the routes of all merchant vessels flying the American flag were strictly controlled by our military and naval authorities. There is no showing that the sailing of the *Malama* was not in conformance with such an order, which would be necessary to establish a deviation from the terms of the articles. The District Court expressly found that the route had been fixed by governmental order (A. 88). Consequently, we submit that the evidence was not only irrelevant to the pleaded issues involved in this litigation but also that it falls far short of establishing a deviation.

**V. The District Court Did Not Err in Denying Libellants Maintenance During Internment by the Enemy.**

As stated at the inception of this brief appellee, in answering the impleading petitions of Matson, denied any liability to Matson, even in the event the latter were held liable on the claims by appellants for maintenance during internment and until their return to the United States. Appellee, however, joins with Matson in denying the latter's liability to appellants for such claims for maintenance and adopts and reasserts the discussion contained in the brief filed by Matson covering this subject. Furthermore, since appellants concede that the claims for maintenance are of the same nature as those pressed in *The President Harrison* and since nothing new is presented by them showing why that decision is improper, appellee rests upon the authority of this Court's decisions in that case as full support of the District Court's conclusion that



appellants in the present case have no right to maintenance during internment.

### CONCLUSION

In conclusion, appellee submits that the only material issue for this Court is whether the contract of hire provided for war bonus during internment on land. Appellee earnestly contends, for the many reasons stated herein, that the contract of hire, consisting of the shipping articles, the riders attached thereto, and the supplementary agreements expressly referred to therein, clearly did not provide for a war bonus during internment on land. Matson has willingly met its obligations under the contract of hire and has paid appellants wages and emergency wages during the full period of internment and repatriation in amounts that range from \$3,665.75 to \$14,473.71 (A. 23, 24). Its rights should now be respected, particularly since the relevant portions of the contract of hire are contained in collective bargaining agreements which representatives of appellants participated in negotiating. Appellee reiterates that these are not the circumstances that invoke the traditional solicitude of the Admiralty Courts for seamen. Appellants have already been paid by Matson compensation benefits for internment that are comparable to benefits paid the vast majority of merchant seamen as well as civilian employees of the United States, and of its contractors, interned during the war. To now grant appellants additional benefits contrary to the express provisions of the contract would not only deny Matson its rights under the contract but would also impose upon appellee, the United States of America, an obligation un-



warranted by the evidence and law applicable to this case and by national policy respecting the great number of other persons similarly exposed to the rigors of internment camps. Consequently, appellee urges that the judgment rendered by the District Court in these cases be affirmed by the Court of Appeals, and that its mandate be issued to that effect.

Respectfully submitted,

FRANK J. HENNESSY

*United States Attorney*

C. ELMER COLLETT

*Assistant United States  
Attorney*

*Proctors for Appellee*

LILLICK, GEARY, OLSON,  
ADAMS & CHARLES,  
JAMES L. ADAMS,  
*Of Counsel.*

**(Appendix follows)**







## **APPENDIX**

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### **SUPPLEMENTARY BONUS AGREEMENT GOVERNING LICENSED PERSONNEL, INCLUDING THE RADIO OPERATOR**

The pertinent portions of the M.M.& P. supplementary bonus agreement are reproduced as an example of a licensed personnel agreement. The agreements of the M.E. B.A. and the A.C.A. are identical.

“(2) War risk areas wherein war risk bonuses shall be paid licensed officers are set forth as follows:

Area I Trans-Atlantic voyages to Spain, Portugal, East, South or West Coasts of Africa, Red Sea, Persian Gulf, India, Iceland and Greenland.

Area II Trans-Atlantic voyages to Russia (Archangel, etc.).

Area III Trans-Pacific voyages to Russia (Vladivostok, Petropavlosk).

Area IV Trans-Pacific voyages to Japan, Philippine Islands, China, Indo-China, East Indies, Malayan Peninsula.

Area V Trans-Pacific voyages to New Zealand or Australia.

Area VI Canada (Atlantic Coast).

“Subject to terms and conditions following, war bonuses shall be paid in the respective areas as above defined, as follows:

Area I (a)  $66\frac{2}{3}\%$  of basic wages for the entire voyage; \$100 for Suez or any other port which is subject to regular bombing, plus



\$5 per day for each day beyond five days that the vessel is in that port; and (b) \$45 for each port in the Red Sea and Persian Gulf not covered in Paragraph (a) supra.

Area II  $66\frac{2}{3}\%$  of basic wages for the entire voyage, and \$75 for each Russian port.

Area III  $66\frac{2}{3}\%$  of basic wages after crossing the 180th meridian, westbound, until recrossing the same meridian eastbound, and \$75 for each Russian port.

Area IV  $66\frac{2}{3}\%$  of basic wages from the crossing of the 180th meridian, westbound, until recrossing the same meridian eastbound.

Area V  $66\frac{2}{3}\%$  of basic wages from arrival of vessel in Suva or the crossing of the 180th meridian, westbound, until departure from Suva or crossing the 180th meridian eastbound.

Area VI 25% of basic wages while vessel is north of 35 degrees of north latitude.

“On round-the-world voyages, westward,  $66\frac{2}{3}\%$  of the basic wages from the crossing of the 180th meridian westbound until arriving in a Continental United States East Coast or Gulf Coast port, or at the Panama Canal. If any vessel referred to in Area I continues eastbound to United States ports via India and the Pacific Ocean said bonus rates for such area will continue until the vessel passes the 180th meridian, eastbound, and thereafter no further bonuses will be payable.

\* \* \* \* \*

“(4) In the event a vessel is interned, destroyed or abandoned as a result of war operations and is unable to continue her voyage, basic wages and emergency wages specified in the collective bargaining agreement between the parties shall be paid to the date that members of the crew arrive in Continental United States ports and the employees shall be repatriated to a Continental United States port.

“While employees are in the war zones areas described herein war bonuses shall also be paid to them at the rate of  $66\frac{2}{3}\%$  of the said basic wages in Areas I to V inclusive, and 25% in Area VI.”



Nos. 12,349, 12,352, 12,350

In the United States Court of Appeals  
For the Ninth Circuit

TIMOTHY E. ARMSTRONG, et al., *Appellants,*  
vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

No. 12,349

JAMES KEITH CURRIE, etc., *Appellant,*  
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MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

No. 12,352

**CONSOLIDATED  
CASES**

DONALD G. STEWART, et al., *Appellants,*  
vs.

MATSON NAVIGATION COMPANY, a corporation,  
*Appellee and Cross-Appellant,*

UNITED STATES OF AMERICA,  
*Appellee and Cross-Appellee.*

No. 12,350

Brief for Appellee and Cross-Appellant  
Matson Navigation Company

**FILED**

DEC 30 1949

**PAUL P. O'BRIEN,**  
**CLERK**

BROBECK, PHLEGER & HARRISON,  
ALAN B. ALDWELL,  
111 Sutter Street,  
San Francisco 4, California,

*Proctors for Appellee and  
Cross-Appellant Matson  
Navigation Company.*





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*Appellee and Cross-Appellee.*

**No. 12,350**

## Brief for Appellee and Cross-Appellant Matson Navigation Company

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### FOREWORD

In each of these consolidated cases, Matson Navigation Company was the respondent in the District Court pursuant to libels filed by the former crew members of the *SS Malama*, a merchant vessel owned by Matson Naviga-

tion Company and operated by it for the United States of America as charterer. These libels asserted claims for bonuses and maintenance during internment of these crew members while on land subsequent to the destruction of the vessel by the armed forces of Japan.

Matson Navigation Company answered the libels and at the same time impleaded the United States of America as a party respondent based upon the charter party provisions whereby the United States of America agreed to indemnify Matson Navigation Company for certain items included in which, it was alleged in the impleading petition, were war bonuses and maintenance claims. The United States of America in its answers to the impleading petitions admitted that as between it and Matson Navigation Company it was liable for any war bonus claims, but denied that it was liable for any maintenance claims.

At the trial, under stipulation of counsel approved by the court, this subsidiary question of the liability for maintenance was deferred pending determination of the issues between the libelants and the respondent. In view of the trial court's decision, it became unnecessary for it to determine this subsidiary question. However, in order to protect its rights in the event of a reversal by this court, and as a precautionary measure, notwithstanding what we conceive to be the true rule that an admiralty appeal is a trial de novo, Matson Navigation Company took cross-appeals from the final decrees adjudging that it recover nothing from the United States of America either on the bonus claim or on the maintenance claim.

In view of the fact that the United States of America admitted that it was liable for bonuses, if any were due,

the burden of presenting the case on this issue has been undertaken by proctors for the United States of America, both in the trial court and in this court. We therefore do not propose to further burden this court with any discussion of this particular issue, but merely wish to make the statement that Matson Navigation Company concurs in and adopts as its own the brief which is being filed on behalf of the United States relative to the bonus issue.

This brief, therefore, will be devoted solely to a discussion of the maintenance issue and very briefly to the cross-appeals.

### ARGUMENT

#### **Appellants Are Not Entitled to Any Recovery for Maintenance.**

It may first be noted that the respective briefs for the appellants cover the maintenance claim in a hap-hazard manner, to say the least. Both briefs indicate that counsel feel that the decision of this court in the *President Harrison* case (*Agnew v. American President Lines, Ltd.*, 177 F.2d 107) is controlling on the question as indeed it is. There is no evidence in the record to indicate that the men were not subsisted by the Japanese during their internment, and in the absence thereof and as pointed out by this court in the *President Harrison* cases, there can be no liability upon the ship owner for such. In view of this court's decision in the *President Harrison* cases, it seems unnecessary to proceed with a lengthy argument on this question. All of the arguments which can be advanced were presented to this court by counsel for American President Lines in the *President Harrison* cases. We think it pointless to take up the time of the court to present those arguments again.



However, counsel for the appellants in the *Armstrong* and *Currie* cases urge an additional reason for the allowance of maintenance, to wit, that a deviation occurred, thereby entitling the seamen to an allowance for maintenance. This theory of deviation was also advanced by counsel for the same appellants insofar as it relates to bonuses and we believe that the point is sufficiently disposed of in the brief for the United States of America. Insofar as it relates to maintenance, we do point out that the cases cited by these appellants do not support the proposition for which they are cited. The cases of *Sheppard v. Taylor*, 30 U.S. 675 and *Turtle v. Northwestern Steamship Company*, 154 Fed. 146, 162 Fed. 256, make no mention whatever of the subject of maintenance and were merely actions, in the first case, for wages only and in the second case for damages. In *The Kentra*, 286 Fed. 163, the vessel was still in existence and the libelant left the ship upon the deviation and the court held he was entitled to wages and damages until repatriated. It is submitted that that is an entirely different proposition from the present case, where the voyage was admittedly frustrated by the loss of the ship. As held in *Newman v. U. S.*, 50 F. Supp. 66, the fact that a seaman may be legally entitled to wages does not mean that he is also entitled to subsistence.

In conclusion, it should be noted that this so-called doctrine of deviation is only advanced by counsel in the *Armstrong* and *Currie* cases. Apparently, counsel in the *Stewart* case do not place any reliance upon it. Furthermore, it should also be noted that deviation was not pleaded in the libels, that no proof whatsoever was adduced at the trial, and finally that the libel in the *Stewart* case bases the claim for maintenance solely on the collective bargaining agreements and not upon the Articles.

## BRIEF ON CROSS-APPEAL

### STATEMENT OF JURISDICTION

The original libels in each of these cases were brought in admiralty by the respective seamen involved and the District Court, of course, had jurisdiction under then Section 41(3), now Section 1333, of Title 28, United States Code. Respondent Matson Navigation Company impleaded the United States of America pursuant to the provisions of the Suits in Admiralty Act, 46 U.S.C. 741, et seq. (Apostles in *Armstrong* case, pp. 27-52<sup>1</sup>). Final decree in all actions which had been consolidated was entered March 24, 1949 (Apostles, pp. 99-102). Notice of cross-appeal was filed in all cases on June 22, 1949 (Apostles, pp. 123-124). Orders allowing cross-appeal in all cases were entered the same day (Apostles, p. 118), pursuant to petitions for cross-appeal, which were likewise filed on that day (Apostles, p. 117). Citations on cross-appeal were likewise served and filed on the same day (Apostles, pp. 121-122). The record was filed and the appeals and cross-appeals docketed in this court on September 12, 1949 (see cover sheet to Apostles).

The appeals were therefore timely taken (28 U.S.C. 2107) and timely docketed (see Order Extending Time for Filing Apostles on Appeal and Cross-appeal filed July 12, 1949, Apostles, pp. 128-129, and as set forth on pages vi and vii of the Appendix to the brief for appellants in the *Armstrong* and *Currie* cases). The jurisdiction of this court to review the final decree of the District Court was therefore sustained by 28 U.S.C., Sections 1291 and 1294.

---

(1) For the sake of brevity, references to the record will be confined to the record in the *Armstrong* case, where the same situation prevails in all cases.

## STATEMENT OF THE CASE

The liability of the United States over to Matson Navigation Company is based upon the charter party of the vessel dated as of November 24, 1941, and the addendum No. 1 thereto dated as of December 20, 1941, which are annexed to the impleading petitions as Exhibit A (Apostles, pp. 31-52). This charter party provided that the United States of America as charterer agreed to reimburse Matson Navigation Company as owner "for its actual out-of-pocket expenses for any war bonuses, extra wages based on the areas to be traversed during, or the ports of call of, the voyage \* \* \* where such bonuses and extra wages are payable by the Owner to the master, officers or crew in accordance with ship's articles or Owner's collective bargaining agreements" (Article 1.06 of Charter) (Apostles, p. 33). The charter party likewise provided, in Article 2.06, that the charterer should pay for "all other charges and expenses whatsoever except those which, by the terms of this Charter, are specifically made payable by the Owner." (Apostles, p. 38). In no place in the charter is it specifically provided that maintenance during internment of the crew on land is payable by the owner, and accordingly it is the contention of Matson Navigation Company that under these provisions, both bonus and maintenance are for the account of the charterer, United States of America.

In view of the fact that the trial court, pursuant to the stipulation of the parties, did not pass upon the liability of the United States to Matson Navigation Company because it held that the libelants were not entitled to recover anything, the Findings and the Final Decree provided that

Matson Navigation Company should not recover anything from the United States of America either for bonus or for maintenance. If this court should reverse the District Court on either the bonus or the maintenance questions, cross-appellant Matson Navigation Company felt that if it had failed to take cross-appeals it might be determined later that it had lost any rights which it might otherwise have had against the United States of America and accordingly these cross-appeals were filed. It should be noted that because of the stipulation of counsel in the trial court, approved by that court, no evidence whatsoever was adduced, nor was this question of subsidiary liability even argued. Accordingly, if this court should reverse the District Court on the question of bonus, it is submitted that it should direct that a decree be entered adjudging that Matson Navigation Company recover from the United States of America any amounts which it is held liable to pay to the respective libelants because the United States admits that it is liable on that issue. If this court should also reverse the District Court on the question of maintenance, then we submit that as no evidence whatever was taken upon this issue, this court should remand the case to the District Court for determination of this subsidiary liability.

We, of course, maintain that the decree should be affirmed in all respects, in which case these subsidiary issues then become moot.

### **SPECIFICATION OF ASSIGNED ERRORS RELIED UPON**

The cross-appellant relies upon both of the two errors assigned, namely No. I and No. II (Apostles p. 126).



**ARGUMENT OF THE CASE**

- 1. In the Event That This Court Should Reverse the District Court on the Question of War Bonus, It Should Direct that the United States of America Be Held Liable to the Cross-Appellant for the Amount Thereof.**

Assignment of Error No. I: "In the event that the Court of Appeals should conclude that libelants are entitled to recover from respondent any sum as war bonus during their internment on land, then the District Court erred in concluding that respondent is not entitled, and in failing to conclude that it is entitled, to recover anything from the impleaded respondent, United States of America, in such respect" (Apostles p. 126).

In view of the fact that the United States admits in its answers to the impleading petitions that it is liable for war bonus (Apostles p. 53), it follows quite naturally that in the event this court should determine any war bonus is payable, it should be held liable to Matson Navigation Company for any sums which it might have to pay to the respective libelants. We note that there is no dispute between Matson Navigation Company and the United States of America on this point, and it seems pointless to argue it any further.

- 2. In the Event That This Court Should Reverse the District Court on the Question of Maintenance, It Should Remand the Case to the District Court for Determination of the Issue of Whether Matson Navigation Company Is Entitled to Recover for Same from the United States of America.**

Assignment of Error No. II: "In the event that the Court of Appeals should conclude that libelants are entitled to recover from respondent any sum as an allowance



for maintenance for any period subsequent to January 1, 1942, then the District Court erred in concluding that respondent is not entitled, and in failing to conclude that it is entitled, to recover for same from the impleaded respondent, United States of America, in such respect'' (Apostles p. 126).

As has been pointed out above in the Statement of the Case, the question of the liability of the United States to Matson for maintenance, if any is recovered by the libelants, was not passed upon by the trial court, no evidence was adduced and no argument was had because of the stipulation of counsel for the respective parties. Accordingly, if this court should conclude that the libelants are entitled to any maintenance, there would be no record upon which it could determine the subsidiary question between Matson Navigation Company and the United States. It seems to us, therefore, that the only logical procedure to follow would be to remand the case to the District Court for the determination of this issue.

**CONCLUSION**

We therefore respectfully submit that the decree of the District Court should be affirmed in all respects, but if this court should reverse the District Court on the bonus issue it should direct a decree that Matson Navigation Company is entitled to recover from the United States of America any amounts which it is held liable to pay for war bonus, and that if this court should also reverse the District Court on the maintenance issue it should remand that phase of the case to the District Court for determination of the issue as to whether the United States of America is liable to Matson Navigation Company for any sums which the latter is held liable to pay for maintenance.

Dated at San Francisco, California,  
December 30, 1949.

BROBECK, PHLEGER & HARRISON,  
ALAN B. ALDWELL,

*Proctors for Appellee and  
Cross-Appellant Matson  
Navigation Company.*

Nos. 12,349 and 12,352  
IN THE  
United States Court of Appeals  
For the Ninth Circuit

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*Appellants,*

vs.

MATSON NAVIGATION COMPANY (a corporation), and UNITED STATES OF AMERICA,

*Appellees.*

No. 12,349

JAMES KEITH CURRIE, as Administrator of the Estate of JACK GEORGE CURRIE, Deceased,

*Appellant,*

vs.

MATSON NAVIGATION COMPANY (a corporation), and UNITED STATES OF AMERICA,

*Appellees.*

(CONSOLIDATED  
CASES)

No. 12,352

APPELLANTS' REPLY BRIEF.

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ALBERT MICHELSON,

Russ Building, San Francisco 4,

*Proctor for Appellants*

JAN 18 1950



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(CONSOLIDATED  
CASES)

No. 12,352

**APPELLANTS' REPLY BRIEF.**

1. THE SHIPPING ARTICLES WERE PLAIN, CERTAIN, AND UNAMBIGUOUS, AND CLEARLY ENTITLED THE LIBELANTS TO WAR BONUS, AT THE RATES STIPULATED THEREIN, COVERING THE PERIOD FROM THE CROSSING OF THE 180TH MERIDIAN WESTBOUND UNTIL CROSSING THE SAME MERIDIAN EASTBOUND.

In the *President Harrison* cases (177 F. 2d 107, 111) this court determined that the shipping article riders there involved entitled the seamen to war bonus at the stipulated rates while they were interned on land west of the 180th meridian. An argument of the appellee therein was that collective bargaining agreements between shipowners and labor unions of which the seamen were members defined "war zones or areas in the terms of voyages" and therefore excluded war bonus for internment on land. (Bf. Appellee, p. 41, *President Harrison* cases.) In holding the argument unsound the court said, 177 F. 2d, at page 109:

"It is a rational interpretation to regard the men, the vessel and the voyage as *not* the *war zone*. Rather each of the three is *in* the war zone. The men remained employees in the war zone during the internment, expressly a contemplated incident of the employment contract."

The riders here involved, unlike the riders in the *President Harrison* case, contain an express agreement in the very first paragraph thereof whereby the shipowner agrees "to pay war risk bonuses to the crew of the SS MALAMA from the crossing of the 180th Meridian Westbound until recrossing the same Meridian Eastbound". (App. Op. Bf. pp. 6, 7.) And the riders here involved, like the riders in the *President Harrison* cases, provided for payment of war

bonus while employees were in a war zone after destruction of the vessel.

Appellees do not contend that the seamen were not entitled to war bonus after the destruction of the *Malama* by enemy action on January 1, 1942, for the 37 days they were interned on the Japanese raider west of the 180th meridian en route to Japan. (A 88, 94-95.) Nor do appellees contend that the seamen were not entitled to war bonus after liberation on or about September 5, 1945, and while they were on vessels *or airships* west of the 180th meridian on repatriation. (A 88, 94-95.) On the contrary, appellees admit the payment of war bonus for such periods and are apprehensive that despite such payments appellants are again claiming them. (Bf. Appellee U.S.A., p. 4.) Apprehension is unnecessary. Appellants' assignments of error leave no doubt that their claim of war bonus is for the period they were interned on land west of the 180th meridian. (App. Op. Bf. p. 12.)

On this appeal the appellees again repeat and elaborate the argument that war zones or areas should be defined in the terms of voyages and war bonus for internment on land thereby excluded. The answer by this court to the same argument in the *President Harrison* cases is equally sound in this case. On the authority of those cases (177 F. 2d 107, 111) a reversal of the decree of the District Court denying appellants war bonus for the period they were interned on land west of the 180th meridian must inevitably follow.

2. THE COURT ERRED IN EXCLUDING EVIDENCE OF THE CONSTRUCTION GIVEN THE SHIPPING ARTICLES BY THE PARTIES AT THE TIME OF SIGNING.

In their opening brief (p. 13) the appellants referred to 45 U.S.C.A., sec. 565. That statute enjoined upon the shipping commissioner the duty of acquainting the master and seamen with the conditions of the riders and ascertaining that they understood them. Appellants offered evidence at the trial to the effect that when the shipping articles were signed questions arose to the meaning of the riders and that the shipping commissioner then explained and construed them. The construction he gave to the riders and announced to the master and seamen was in accord with the reasonable construction thereof for which appellants contend and in accord with the construction given by this court to similar riders in the *President Harrison* cases. The court excluded such evidence. The cited statute will not permit it to be doubted that the court erred in thus ruling. Nowhere in the briefs for appellees is the said statute referred to or considered.

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3. THE COURT ERRED IN EXCLUDING EVIDENCE OF CONTEMPORANEOUS ORAL CONTRACT BETWEEN THE PARTIES FOR PAYMENT OF WAR BONUS FOR PERIOD OF INTERNMENT ON LAND.

The present cases were tried before the decision of this court in the *President Harrison* cases. The trial judge was then committed to the view that neither the riders nor the collective bargaining agreements stipulated for payment of war bonus while the seamen were



interned on land. (*Agnew v. American President Lines, Ltd.*, 73 F. Supp. 944.) It was plain that the master and the seamen signed the shipping articles of the *Malama* on the understanding that the seamen would be paid war bonus for whatever period they might be interned on land west of the 180th meridian. It was equally plain that if the riders did not create a contract of that character then the master and the seamen made a collateral one to that effect with the approval of the shipping commissioner and it became a part of the shipping articles. The proctor for the appellants believed and still believes that in a court of admiralty where seamen are traditional wards the evidence offered should have been admitted. The authorities cited in the opening brief at pages 14 and 15 confirm that belief. *The Kambira*, C.C.Ala., 100 F. 118-119, may be added.

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#### 4. THE COURT ERRED IN EXCLUDING EVIDENCE OF DEVIATION OF VOYAGE.

The *Malama* arrived at Honolulu after Pearl Harbor and the declaration of war against Japan and then sailed for New Zealand. It is idle for any one to contend that this was not a deviation from the voyage stipulated in the shipping articles. That the evidence of deviation was material to the issue that the seamen were entitled to war bonus while interned on land west of the 180th meridian seems clear.

5. **THE COURT ERRED IN DENYING THE MOTION OF LIBELANTS TO SET ASIDE THE SUBMISSION AND REOPEN CAUSE FOR THE INTRODUCTION OF FURTHER PROOF.**

This subdivision was sufficiently developed in the opening brief at pages 15 to 18. Appellees have not questioned the authority of the cases there cited or attempted to distinguish them. Error in the ruling of the court was there fully demonstrated.

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6. **THE DISTRICT COURT ERRED IN DENYING LIBELANTS ANY RECOVERY FOR MAINTENANCE.**

At pages 35 and 36 of its brief, the appellee United States of America states:

“\* \* \* since appellants concede that the claims for maintenance are of the same nature as those pressed in *The President Harrison* and since nothing new is presented by them showing why that decision is improper, appellee rests upon the authority of this Court’s decision in that case as full support of the District Court’s conclusion that appellants in the present case have no right to maintenance during internment.”

Appellee’s statement of appellants’ position is inaccurate. A new element has been added for the consideration of the court on this appeal with respect to maintenance. Under the doctrine of deviation of voyage appellants would be entitled to maintenance during the period of their internment on land and in fact from the date of their capture by the Japanese. The cases cited at page 19 of appellants’ opening brief

remove any doubt on the subject. Appellants invoked and again invoke that rule.

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**7. LIBELANTS ARE ENTITLED TO INTEREST AND COSTS.**

Appellees have not challenged the soundness of this assignment if the decree be reversed. Appellants again assert it.

---

**CONCLUSION.**

Appellants again respectfully submit that the decree of the District Court should be reversed with direction to enter judgment for libelants together with interest and costs.

Dated, San Francisco,  
January 16, 1950.

ALBERT MICHELSON,  
*Proctor for Appellants.*















